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ABSTRACT

This book is designed to serve as a comprehensive resource on all aspects of school finance for Pennsylvania educators. Chapter 1 provides a historical overview of Pennsylvania school finance. The next three chapters examine the local, state, and federal sources of revenue. The fifth chapter explains the components of Pennsylvania's mandatory system of school-district accounting, and the sixth chapter describes financial management and planning. Chapters 7 and 8 examine developing a budget cycle and conducting district audits. The ninth chapter discusses fiscal administration--its roles, duties, and activities, and the final chapter offers a historical overview of distressed school districts. Appendices contain a bibliography, the Pennsylvania Public School Code of 1949, samples of policies, vital statistics on budget decisions, a sample budget review and analysis, guidelines for auditing student-activity funds, and a glossary. (LMI)

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Understanding School Finance

A Basic Guide for Pennsylvania School Directors

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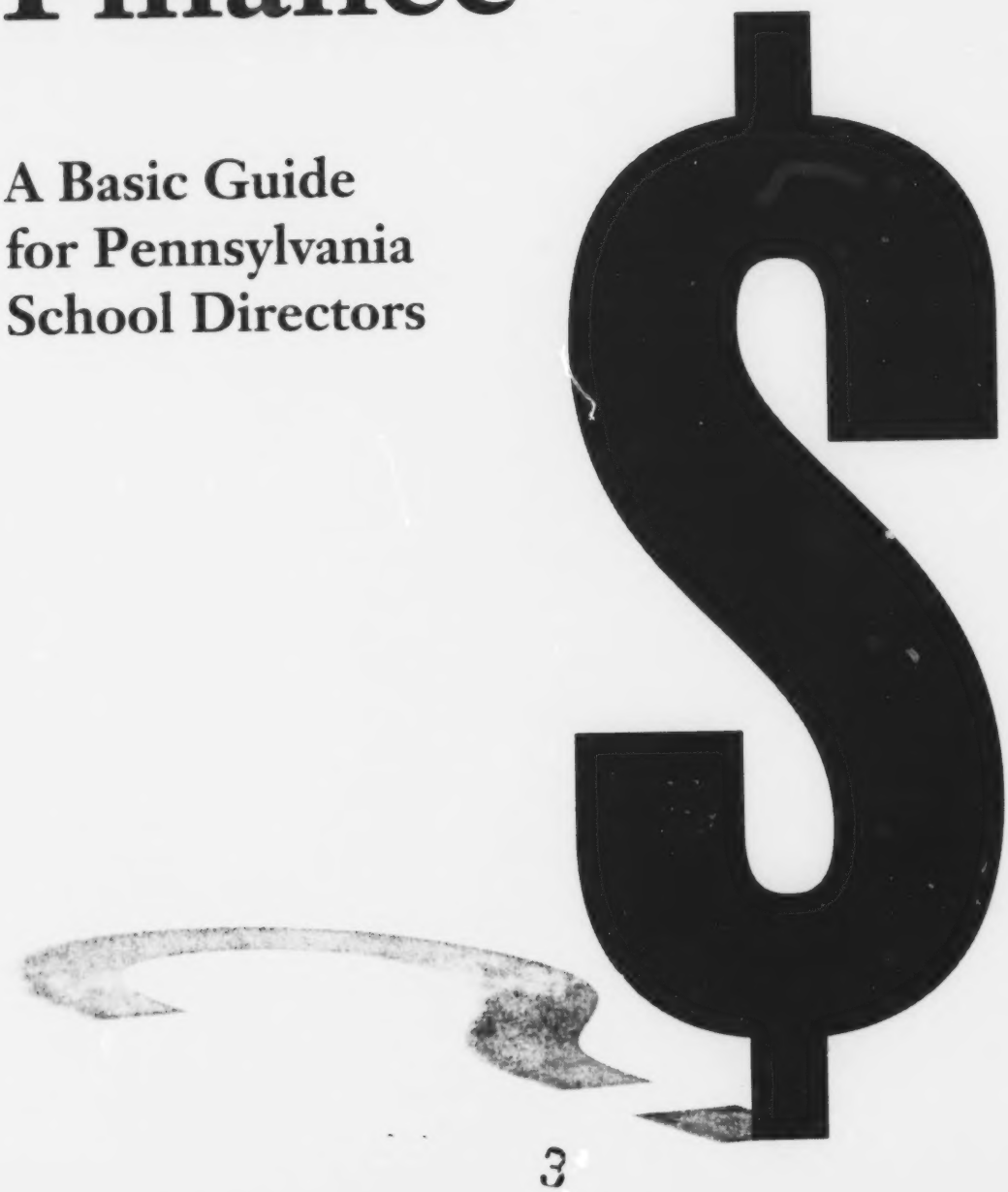
Understanding School Finance

A Basic Guide for Pennsylvania School Directors



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Preface

Understanding School Finance is a comprehensive resource on all aspects of school finance. It is written in easy-to-understand language for use by school directors, school officials and others interested in Pennsylvania school finance.

School finances are complex, but absolutely essential for public education. This edition of Understanding School Finance is a complete rewrite of the previous edition (1987). The chapter on local revenue includes detail about the Act 511 taxes. State funding covers the foundation funding formula. New chapters on budgets, audits and auditors and distressed school districts have been added.

Other chapters include the role of financial planning, budgets, the accounting system and a variety of other financial topics.

The Pennsylvania School Boards Association presents this handbook to enable school directors to achieve a broad overview and clear comprehension of school finance. We hope that you find this PSBA service helpful in your role in public education.

Joseph V. Oravitz
Executive Director

Acknowledgments

Understanding School Finance is designed to serve as a guide for Pennsylvania school directors and others interested in public school funding. Along with historical considerations, the various elements of financial management are presented in this handbook, expanding on the 1987 edition.

PSBA is grateful to those who contributed to this completely revised handbook. **David W. Davare PhD,** PSBA director of research, served as project director. **Lynn H. Mannion,** PSBA assistant executive director for communications, served as editor.

Others who contributed to the content, were: **Charles Hoffman,** chief, Municipal Statistics and Information Division, Pennsylvania Department of Community Affairs (Chapter 2); **Edward R. Kealy PhD,** director of Federal Programs, National School Boards Association (Chapter 4); **Anna Maria Anderson,** division chief, school finance, Pennsylvania Comptroller's Office (Chapter 5); and **Ronald Stainbrook EdD,** chief, Office of Management Assistance, Pennsylvania Department of Education (Chapter 10). Special thanks to **David Sallack,** executive director of the Pennsylvania Association of School Business Officials, and to **William Martin EdD,** Pennsylvania Auditor General's Office.

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Table of Contents

CHP 1 – OVERVIEW OF SCHOOL FINANCE 1

- Early History
- The Subsidy System
- AIE/WADM
- Foundation Funding
- History of Local Taxation
- Act 511 Taxes
- Property Tax Dependence
- School District Taxing Authority

CHP 2 – LOCAL REVENUE 11

- Local Control
- Real Property Taxes
- Assessment Function
- Non-property Taxes
- Earned Income Taxes
- Tax Rates
- Taxable Income
- Per Capita Taxes
- Occupation Taxes
- Assessment of Occupations
- Occupational Privilege Taxes
- Reality Transfer Taxes
- Business Gross Receipts Taxes
- Amusement/Admissions Taxes
- Mechanical Devices Taxes
- Other Taxes

CHP 3 – STATE FUNDING 39

- Calculating State Subsidies
- Vocational Education
- Pupil Transportation
- Special Education
- Intermediate Units
- School Construction
- Retirement and Social Security
- School Health Services

- Nonpublic Schools
- Other State Subsidies

CHP 4 – FEDERAL REVENUE 55

- Basis of Federal Role
- Vocational Education
- School Lunch Program
- Impact Aid
- National Defense Education Act
- Elementary and Secondary Education Act
- Education Consolidation and Improvement Act
- Other Major Programs
- Changing Federal Role

CHP 5 – ACCOUNTING IN SCHOOL DISTRICTS 65

- Overview of the Accounting System
- Accounting and Reporting Standards for LEAs
- Fund Balance
- Important Elements of the Accounting System
- Revenue Dimensions
- Revenue Coding Example
- Expenditure Dimensions
- Expenditure Coding Example
- Balance Sheet Dimensions
- Balance Sheet Coding Example

CHP 6 – FINANCIAL MANAGEMENT AND PLANNING 77

- Financial Plan
- Why Plan
- Leading the Process
- Using a Committee
- Benefits of Planning
- Realistic Expectations
- Keeping on Target

CHP 7 – THE BUDGET 85

- A Budget is Not . . . .
- Authority
- Budget Policy
- More Benefits of Budgets
- Roles in Budget Preparation
- Board Members
- Superintendent's Role
- Chief Business Official
- Budget Cycle and Timelines

- Preparation of the Budget
- Adopting the Budget
- Budget Execution

CHP 8 – AUDITS AND AUDITORS 101

- Selection of Auditors
- Request for Proposals
- Different types of Audits
- Purpose of Audits
- Audit Reports

CHP 9 – FISCAL ADMINISTRATION 107

- Roles and Duties
- Financial Activities
- Tax Collection and Collectors
- Bonding
- Construction of Facilities
- Capital Budgeting
- Insurance Programs
- Financial Records

CHP 10 – A HISTORY OF DISTRESSED SCHOOL DISTRICTS 119

- Origin of a Problem
- Grants in Aid
- Special Tax Levy Authorization
- Definition of Distress
- Reductions in Distressed Districts
- Recent Developments
- Criteria to Determine Distress
- Powers and Duties of a Board of Control

APPENDIX 125

- Bibliography
- Pennsylvania Public School Code of 1949
- Exhibit 1 – Sample Policies
- Exhibit 2 – Vital Statistics on Budget Decisions
- Exhibit 3 – Budget Review and Analysis
- Exhibit 4 – Guidelines for Auditing Student Activity Funds
- Glossary

Overview of School Finance

EARLY HISTORY

The first permanent settlements in Pennsylvania were along the west bank of the Delaware River. About 1,000 people, mainly Swedes, Dutch and English, began to arrive in 1640. The first schoolhouse was erected in 1682.

Early education was placed in the hands of the church and remained largely sectarian until the late 1700s. A provisional constitution, signed in Philadelphia in 1776, contained an education section stating: "A school or schools shall be established in each county by the Legislature, for the instruction of youth, with salaries to the masters paid by the public . . ."

The initial reference to free education is found in Pennsylvania's Constitution of 1790, mandating public schools so "the poor may be taught gratis."

The initial reference to free education is found in Pennsylvania's Constitution of 1790, mandating public schools so "the poor may be taught gratis." Four years later, the House of Representatives adopted a plan for funding these schools, with 20% of the costs paid from the state's General Fund and the remaining 80% supported by county taxes.

So began not only the public school system, but also a partnership of state and local funding. That partnership has continued uninterrupted, but has changed significantly.

A legislative battle for free schools in the commonwealth began in 1830, when George Wolf, a former teacher and a bold supporter of education, was governor. A committee report submitted to the Legislature chastised the body for inactivity in the field of education. As a result, in April 1831,

the Legislature passed the Common School Fund Act and a funding start began. However, it took another three years for the legislation to establish a system of education via common schools.

The act of 1831 established funds of $2 million. The Free School Act of 1834 provided, "the city and county of Philadelphia and every other county in the commonwealth and every ward, township and borough . . . shall form a school district." The 1834 act provided for school boards and county taxes to be voted on by a committee of the county commissioners, as well as one delegate school board member from each county board. A county school tax of not less than twice the amount received from state aid was mandated. Further, the 1834 act provided that negative voting districts were to receive no state aid.

In 1835, state appropriations were distributed through the county treasurer, based on the number of taxable inhabitants. County treasurers then distributed the money. Superintendents constantly complained that the method was inequitable because it favored more populated areas and wealthy counties, while disregarding the number of children.

Even though the act passed almost unanimously, it immediately ran into trouble from the wealthy who disassociated themselves from the "common" or "poor." Schools in Pennsylvania had always been free, but not always compulsory.

Districts conformed to political subdivisions, and the concentration of all the most essential powers existed in locally elected school boards. Further, the commonwealth never limited schools to elementary branches, encouraging high schools and universities.

In 1835, state appropriations were distributed through the county treasurer, based on the number of taxable inhabitants. County treasurers then distributed the money to the different districts, also based on the number of taxables.

Distribution of funds using this formula continued for 63 years. During this time, superintendents constantly complained that the method was inequitable because it favored more populated areas and wealthy counties, while disregarding the number of children.

The Appropriations Act of 1863 provided distribution based on the number of children attend-

ing a school. This was the first use of "average daily membership." Distribution, based on children, was so difficult that no funds were paid for one year. The lack of payment resulted in the Legislature being reconvened and restoring the old basis.

A new system for disbursing state aid began in 1897, using the number of children ages 6-16, the number of taxables and taxable residents.

Numerous funding changes quickly followed. In 1903, the first law setting a minimum teacher salary ($35 per month) was passed. In 1907, the minimum pay was raised to $40 per month for teachers with provisional certificates. In 1911, taxable inhabitants were deleted from the subsidy formula. The Woodruff Salary Act of 1919 provided for a range of reimbursements based upon classification of certificates.

Economic and political factors soon influenced public education as much as, if not more than, theorists would. World War I accelerated the transition to an industrial society and ended much of the rural isolation. The Great Depression had a singular impact on school finance. In 1930, 82% of local school costs were funded almost exclusively by local property taxes. As these became uncollectable, state aid jumped to almost 30% in 1940, and to 40% by 1950.

THE SUBSIDY SYSTEM

During the 1950s, attention was focused on expansion of the local tax base and strengthening subsidy and other assistance efforts. The launch of Sputnik I in 1957 cleared the way for a federal role in the funding of public schools, initially for reasons of national defense.

From these developments, Pennsylvania's subsidy system emerged as an attempt to equalize the financial resources available to school districts. Through an intricate formula, state aid is apportioned so that relatively poorer school districts receive greater assistance than wealthier ones. The means of accomplishing this purpose has undergone a number of changes in recent years

and continues to be affected by the levels of funding actually provided by the General Assembly.

Subsidy payments were made on the basis of teaching units prior to 1968. Teaching units were considered to be 35 elementary or 22 secondary students. Act 96 of 1968 introduced the "weighted pupil" factor in disbursing state aid, establishing a cost differential for educating kindergarten, elementary and secondary students.

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A district's Weighted Average Daily Membership is calculated by multiplying the number of students enrolled by the appropriate factor for each: kindergarten 0.5, elementary 1.0, secondary 1.36. Thus, two school districts with the same number of students, but with different totals in the various grade levels, would have different WADMs.

The process determines a district's theoretical need related to wealth and, therefore, its relative need for state financial assistance. This resulted in the development of the Market Value Personal Income Aid Ratio, commonly known as aid ratio. The aid ratio was intended to be a reflection of a district's ability to raise local revenues. Both real property market value and personal income were used in determining the theoretical tax-raising ability. In computing the aid ratio, property market value was given a 60% weighting and personal income was weighted at 40%.

It should be emphasized that these calculations were intended to equitably distribute the basic instructional subsidy. As will be discussed later, additional aid was available for other special needs. This basic subsidy determined the state's share of a district's Actual Instructional Expense. As a means of comparison with other districts, this was prorated by Weighted Average Daily Membership to show instructional costs per student, and resulted in the AIE/WADM.

AIE/WADM

Act 59 of 1977 introduced two additional concepts. Base Earned for Reimbursement, the maximum amount a district could be paid under the basic instructional subsidy, provided a series of computations that could result in 201 separate reimbursement levels. The statewide maximum reimbursement was the median (midpoint) AIE/WADM among the state's school districts, and the minimum level of state per-pupil aid was the median less $200. This calculation was deleted from the subsidy formula.

Under the Equalized Subsidy for Basic Education, the calculation of equalized mills was used in determining only a small amount of the total aid appropriated by the General Assembly. Most subsidy funds were distributed on the basis of a formula that included aid ratio, WADMs and a fixed dollar amount per pupil, known as the Factor for Educational Expense.

Most state aid to public education was paid through the Equalized Subsidy for Basic Education. There were a variety of special funding programs to compensate for needs peculiar to specific districts. These needs included:

- School building construction.
- Pupil transportation.
- Homebound instruction.
- Driver education.
- Special education.
- Pupil health services.
- Density-sparsity.
- Poverty payments.

FOUNDATION FUNDING

Beginning in the late 1980s, increasing pressure on local tax bases coupled with changing economic conditions resulted in demands for an examination of the funding system. In 1992, the House Appropriations and Education committees commissioned

a study of the way Pennsylvania funds elementary and secondary education. As a result of the study, the Legislature, with the support of the governor, implemented a new funding program.

The new program became effective for the 1993-94 school year. Known as foundation funding, it established a specified level of per pupil spending (1993-94 = $3,875). The concept is to establish state support based on a minimum level of spending. Minimum spending would then be enhanced by local resources to satisfy locally determined needs.

Foundation funding established a specified level of per pupil spending. The concept is to establish state support based on a minimum level of spending, Enhanced by local resources to satisfy locally determined needs.

It is anticipated that foundation funding will go through several changes during the first few years of its existence. However, local support of public education costs will continue to be an important element in Pennsylvania.

From the beginning, the state's public school system has been supported by local taxpayers. Local support has been essential to provide necessary resources for instruction and support services. The state's primary funding role is intended to ensure an equitable distribution of resources among districts of widely varying wealth – not to replace or supplant local funding.

The General Assembly's constitutional duty to maintain and support a system of public education has been delegated to local school boards. Additionally, this delegation includes the authority to levy taxes to help support the schools they administer.

HISTORY OF LOCAL TAXATION

Local taxation has the same early roots as education. In Pennsylvania, local taxation was influenced by the English. The theory of English taxation is derived from the economic concept of value, based on land, labor and capital. Local taxation was initially focused on land through the real estate tax, and labor through occupation assessment and income taxes.

Authority for school districts to levy property taxes is a part of the Public School Code of 1949. Local taxation is also consistent with the early growth of education. Non-property taxes first appeared under the Sterling Act of 1932 in Philadelphia. Following World War II, as the population began migrating into the rural (soon to be suburban) areas, local governments sought expanded authority to generate revenue to meet growing demands for services. In response to this demand, the Legislature passed Act 481 of 1947, known as the "Tax-Anything Law" because of the broad authority granted to local governments and school districts. In 1965, the Legislature re-enacted the tax authority as Act 511 of 1965 – the Local Tax Enabling Act – which remains as the single largest alternative to property tax for school districts.

ACT 511 TAXES

Act 511 authorizes the levying of earned income, occupation, per capita and other taxes within certain limits. In total, these levies may not exceed the equivalent of 12 mills of real estate taxes for the taxing body. Whenever two coterminous political subdivisions (a school district and municipality) impose any one of the taxes authorized by Act 511, proceeds must be shared equally unless otherwise agreed upon. Each, however, is entitled to claim up to one-half of the limitation for each tax.

In addition to Act 511, school taxing powers are governed by the School Code. Specifically, Section 679 authorizes a per capita tax not to exceed $5 for each resident over age 18. The code also provides for school property taxes. There is a 25-mill limit for general school purposes, except in Philadelphia and Pittsburgh.

The limitation of Section 672 also authorizes additional property tax – unlimited in amount – to pay for salaries, building rentals, sinking fund charges and amortization of bond issues. In effect, school districts are not restricted in the use of the property tax.

Statewide, the property tax accounts for more than 75% of local taxes collected by school districts – about one-third of the total support of public education.

PROPERTY TAX DEPENDENCE

Are schools too dependent upon the real estate tax as a source of revenue? That question has recurred frequently over the past two decades and is based on the lack of relationship between education and the property base that supports education.

Reliance upon property tax is due to the ease of collection (compared with per capita and "nuisance" taxes). Another reason for reliance upon the property tax is the absence of a real limit on dollars generated. Use of this tax is criticized because of the inadequate county-level assessment systems upon which it is based.

Perhaps the best-known attacks on the real estate tax were those waged by civil rights advocates in the late 1960s and early 1970s, challenging the constitutionality of the levy. These suits claimed the property tax was discriminatory due to the variance in the wealth of school districts.

Two heralded cases on this issue were *Serrano v. Priest* and *Rodriguez v. San Antonio School District.* In the former, the California Supreme Court found that the state system of school finance "invidiously discriminates against the poor because it makes the quality of a child's education a function of the wealth of his parents and neighbors." In the latter, the Texas system of property tax revenue distribution was challenged in the state courts and before the U.S. Supreme Court.

The cases raised expectations that the courts would rule the property tax unconstitutional for support of public education. In fact, much of the publicity at the time appeared to indicate that this, indeed, had happened. However, upon review, it is clear that the courts have neither dismantled nor even affected the property tax.

Shortly after rendering its opinion in *Serrano,*

the California Supreme Court issued an unusual clarification. The court emphasized that it has not found the property tax itself unconstitutional but, rather, its application as an element of the state's system of funding public education was found unconstitutional. In *Rodriguez*, the U.S. Supreme Court eventually decided against upsetting the Texas school finance system.

In an earlier case, *McInnis v. Ogilvie*, the high court affirmed a lower court decision upholding challenged school funding methods: "Unequal educational expenditures per student, based upon variable property values and tax rates of local school districts do not amount to invidious discrimination."

Pennsylvania ranks near the bottom of the list of states in terms of uniformity of assessment. When subsidy aid is not appropriated to fully fund the ESBE formula, an increased financial burden is carried by local property taxpayers.

The bottom line in these cases is not the equity of the property tax, but the equity of the total school funding system. If a state's public education program is too dependent on the property tax levy, then the question of discrimination is valid. However, if other revenues counter the imbalances in this tax, there is no constitutional issue.

Pennsylvania's reliance on the property tax for public schools compares well with other states. The Pennsylvania Tax Commission, in its 1981 report, noted that 35 states were more dependent upon real estate tax to finance education. The commission report concluded that the commonwealth had been "about average in terms of proportion of revenues for school districts that is derived from the property tax."

In recent years, much of the controversy surrounding the school property tax can be traced to absence of statewide standards for assessment practices and insufficient state funding for the basic school subsidy. Pennsylvania ranks near the bottom of the list of states in terms of uniformity of assessment. When subsidy aid is not appropriated to fully fund the ESBE formula, an increased financial burden is carried by local property taxpayers.

These problems have been exacerbated by

reductions in federal funding for education, which require state and local revenues to support even more of the cost of operating public schools.

SCHOOL DISTRICT TAXING AUTHORITY

Taxing authority applies to all school districts, except Philadelphia, Pittsburgh and Scranton.

Act 511 taxes
Per Capita $10
Occupation (Flat Rate) $10
Occupation (Millage) no limit
Occupational Privilege $10
Earned Income 1%
Deed Transfer 1%
Mechanical Devices no limit
Amusement 10%
Business Gross Receipts 1 mill wholesale
1 1/2 mills retail
no limit other businesses

Authority to levy a business gross receipts tax was repealed by the Tax Reform Act of 1988. The repeal "grandfathered" existing levies but permitted no new or increased levies after Nov. 30, 1988.

Chapter 2

Local Revenue

LOCAL CONTROL

Pennsylvania's public education system is based on local control, to ensure that schools meet the unique demands of the communities they serve. At the same time, schools must comply with state mandates. Such dual nature is also reflected in the financing of schools. This chapter examines the various sources of revenue that are available to local districts.

Local taxation powers are the most direct aspect of Pennsylvania's long tradition of local control. All citizens are expected to support their local schools through taxation. The intent is for the community to make an investment in the educational system that serves them and the state.

Local taxation powers are the most direct aspect of Pennsylvania's long tradition of local control. The intent is for the community to make an investment in the educational system.

In view of the local contribution element of school financing, the General Assembly has delegated broad taxing powers to local school boards. Such delegation is found in two places. Authority to levy real property tax is part of the Public School Code, which also authorizes a per capita tax. Act 511 of 1965, the Local Tax Enabling Act, authorizes local school districts to levy a variety of non-real property taxes. The authority to levy taxes is the sole discretion of the local district without approval of any other government unit.

Philadelphia, with the only appointed school board in the state, is the one district where taxation is subject to municipal oversight. In all other districts, spending and taxation decisions of local elected school directors are final and binding.

The General Assembly delegated extensive authority to local boards of directors to provide

for educational needs in their districts. The delegation, found in Section 507 of the School Code, provides:

In order to establish, enlarge, equip, furnish, operate and maintain any schools or departments herein provided, or to pay any school indebtedness which any school district is required to pay, or to pay any indebtedness that may at any time hereafter be created by any school district, or to enable it to carry out any provisions of this act, the board of school directors in each school district is hereby vested with all the necessary authority and power annually to levy and collect, in the manner herein provided, the necessary taxes required, in addition to the annual state appropriation, and shall have, and be vested with, all necessary power and authority to comply with and carry out any or all provisions of this act.

Under the authority of Section 507, along with the sections on real property taxes, per capita tax and Act 511 of 1965, local districts generate sufficient revenue to operate.

REAL PROPERTY TAXES

The largest source of local tax revenue for school districts in Pennsylvania is the real property tax. Real property tax is also known as real estate tax. For the 1990-91 school year, real estate taxes accounted for 78.6% of locally generated revenues and 43.3% of all revenues received by the 501 school districts.

Authority to levy a tax on real property is found in Section 672 of the School Code, with a stated rate of 25 mills on assessed value of taxable real property within the district. However, this section was amended to provide an additional tax on real estate. The additional tax rate is unlimited to pay for salaries, building rental, sinking fund changes connected with building projects, and the amortization of a bond issue. These exceptions to the stated limit constitute the major expenditures of

school districts. The practical effect of the amended authorization is to remove a ceiling on the real property tax rate for school purposes.

School boards are authorized to fix the rate (or millage) on assessed value. However, they are dependent upon county government to prepare and maintain property valuation records. In April of each year, county assessment officials furnish to school districts, at county expense, a tax duplicate reflecting the latest adjusted values of taxable real estate in the district. Relying upon this information, school directors determine the appropriate millage rate to generate sufficient revenue to meet district needs.

School boards are authorized to fix the rate on assessed value. However, they are dependent upon county government to prepare and maintain property valuation records.

One mill of tax is equal to $1 for every $1,000 of assessed value. Calculation of the millage rate can best be explained by the formula, Millage Rate = (Required Revenue/ Assessed Value) x 1,000.

Required revenue is the difference between estimated total expenditures and estimated revenue from all other sources. Assessed value is the certified taxable assessed valuation provided by the county. The above formula does not reflect adjustment for delinquencies or the required discount.

Before a tax levy is final, public notice must be provided at least 30 days prior to enactment of the tax levy resolution. Real estate tax rates must be enacted every year. However, for Act 511 and per capita taxes, once enacted, the rate remains in effect until changed.

Once the tax rates are established, a tax duplicate is issued to the tax collector. This duplicate is the collector's authority to receive tax revenue. Normally, this tax duplicate is for one year; however, it remains valid until a complete settlement is made. Unpaid real property taxes are collected for school districts and other local taxing jurisdictions by county tax claim bureaus.

The School Code also addresses the unique needs of school districts that cross county lines, a

situation that affects about 90 of the state's 501 school districts. The law establishes several specific procedures for equalizing real property taxes in these districts.

Generally, all land and buildings are subject to local property tax levies, unless specifically exempt. The Pennsylvania Constitution exempts property owned by disabled war veterans or their widows. The assessment laws exempt the following categories of property:

1. Churches or other places of worship.
2. Burial places not held or used for private profit.
3. Hospitals, universities, colleges, seminaries, academies, associations and institutions of learning, benevolence or charity.
4. Schoolhouses belonging to any county, borough or school district.
5. Courthouses, jails and poorhouses.
6. Nonprofit public parks.
7. All public property used for public purposes.
8. Property owned, occupied and used by a veterans' organization.
9. Property owned and actually and regularly used by purely public charitable institutions.
10. Playgrounds founded and maintained by public or private charity.
11. Free public libraries.
12. Museums, art galleries and concert halls provided and maintained by public or private charity for public use if not operated for profit.
13. Farm silos.
14. Machinery, tools, appliances and other equipment contained in industrial establishments.
15. Residential construction in certain circumstances.

Tax exemption has to be requested by real estate owners, who must demonstrate that their properties are eligible to be removed from tax rolls based on the criteria established by law.

Public utilities are not required to pay local property taxes on their facilities. However, those

entities are subject to the Public Utility Realty Tax Act, a state levy which generates revenue that, in turn, is distributed to political subdivisions in lieu of direct local taxes on utilities.

School property taxes are affected by a variety of other state laws as well. The Senior Citizens Rebate and Assistance Act provides state lottery-funded rebates for property taxes and that portion of rent attributable to property taxes. These rebates are paid directly to the individuals. Senior citizens, widows, widowers and permanently disabled people with income below specified levels are eligible for the rebates. The program is designed to help make the property tax less regressive and onerous for lower-income taxpayers. Individuals must apply annually to participate in this program.

Special laws also have enabled farmers and other owners of agricultural and forest lands or other "open spaces" to be protected from high real property taxes – the Covenant Preserving Land Uses Act of 1966 and the Pennsylvania Farmland and Forestland Assessment Act of 1974 (the "Clean and Green" Law).

In other areas, laws have provided tax incentives to improve property in designated areas. The Improvement of Deteriorating Real Property or Area Tax Exemption Act and the Local Economic Revitalization Tax Assistance Act authorize school boards and municipal governing bodies to exempt from taxation certain improvements made to properties in specified neighborhoods or areas on established schedules.

Because school boards and municipal governing bodies use the real property tax, the General Assembly has established a system of administering that tax which applies to all those jurisdictions. A central element of the system is the assessment process, which is the basis for determining a property's value and, hence, its tax liability.

ASSESSMENT FUNCTION

Revenue from the property tax is generated by a levy (millage) on assessed value of real property.

Determination of the assessed value is the responsibility of county government. Counties are required by law to accomplish several tasks related to valuation for tax purposes: determine an actual (market) value, determine the portion of the value to be used for tax base, and provide for adjustments.

Revenue from the property tax is generated by a levy (millage) on assessed value of real property. Determination of the assessed value is the responsibility of county government.

Determination of value can be accomplished by several different methods. The most common are either estimated market value or construction value. Actual determination also requires establishing a base year; the market value approach estimates the value of property through property appraisal techniques. Construction value uses building costs on a per- square-foot basis. Because market and construction values change over time, a base year is selected and all values are determined using the base year values. This means, if a property is constructed in 1990 and the base year is 1960, the appraiser must use the same method and price scale used in 1960. *(Note: the market value established for assessment is not the same as the market value calculated by the State Tax Equalization Board and used by the Department of Education for aid ratio or equalized millage calculations.)* The proportion of value for tax purposes is determined by applying a percentage rate to the determined market value. This percent is referred to as the predetermined ratio. The ratio is set by county commissioners and can be as low as 1% or up to 100% as authorized by assessment law. *(Note: fourth through eighth class counties are limited to 75% predetermined ratios.)*

Providing for adjustments requires that the assessment function adapt to changes, such as additions and deletions, and challenges to value from owners/interested parties up to and including reassessment. While additions, deletions and appeals are mandatory, reassessment is local choice.

In Pennsylvania there are a number of different laws concerning specific actions. However, each law contains the three requirements. These laws are: General Assessment Law, First Class

County Assessment Law, Second Class County Assessment Law, Second Class A and Third Class County Assessment Law, Fourth through Eighth Class County Assessment Law and Third Class City Assessment Law. When the General Assessment Law conflicts with one of the other laws, the specific law applies.

Assessment law clearly creates a climate of local control. Under the various laws, boards are established to regulate and supervise assessments in the county. Board membership is either the elected county commissioner or designee, as provided by the specific law. County commissioners are also responsible for appointing the county assessor.

The Pennsylvania Constitution, in Article VIII, Section 1, requires that all taxes must be uniform on the same class of subjects within the territorial limits of the authority levying the tax. That mandate renders the assessment function important.

School boards and other local taxing entities are considered to be parties to all assessment appeals. This legal standing enables them to participate in the process of equalizing assessments or revising property values.

School boards and other local taxing entities are considered to be parties to all assessment appeals. This legal standing enables them to participate in the process of equalizing assessments or revising property values. In all cases, however, those decisions finally rest with county governments or, ultimately, with the courts. The process is encumbered by often conflicting provisions of various laws and a lack of uniformity in assessments and no statewide standards.

Pennsylvania's system of assessment ranks among the least efficient of the 50 states. Local control and lack of state standards result in confusion and inconsistency in assessment practices among the 67 counties.

In fact, much of the criticism of the property tax can be traced to underlying inequities in assessment methods. Among the leading problems, as identified by the Pennsylvania Tax Commission in 1979, are: lack of objective standards and performance criteria; absence of incentives and penalties for county assessment offices; and disparity of

'25

resources available to those offices. Reassessments are conducted only sporadically and usually are not updated for years after being completed.

This assessment system actually has a major impact on a number of school taxes because basic information required to levy several of the non-property taxes is provided by county assessment officials.

NON-PROPERTY TAXES

Revenue generated by non-property taxes is smaller than that generated by the property tax; but, non-property tax revenue still generates a significant level of revenue to support education. During the 1990-91 school year, non-property tax revenue accounted for more than 15% of total local revenue or about 20% of total real estate tax revenue. These sources include taxes on earned income, occupations, amusements and businesses.

This revenue source is authorized primarily by Act 511 of 1965, the Local Tax Enabling Act. Act 511 was a reenactment of Act 481 of 1947, often referred to as the "Tax-Anything Law."

Over the years, Act 511 has been amended. The amendments usually limited the sweeping grant of powers provided by the act. The act authorizes specific authority and limits for a number of taxes; other taxes are levied under the general grant of power. Most of these sources are described in the following sections, which have been excerpted with permission from: *Taxation Manual, Sixth Edition, Pennsylvania Department of Community Affairs, Harrisburg, PA, January 1993. (A copy of the publication is available to school districts and municipal governments without charge from Publications Office, Department of Community Affairs, P.O. Box 155, Harrisburg, PA 17108.)*

EARNED INCOME TAXES

Local income taxes in Pennsylvania are variously termed earned income taxes, wage taxes, net profits taxes or a combination of these terms. Local

income taxes provide the chief source of nonproperty taxation for municipalities and school districts.

Local income taxes were first authorized for Philadelphia in 1939, making it the first municipality in the United States with a local income tax.

The Local Tax Enabling Act (Act 511 of 1965) authorizes local earned income taxes for other municipalities and school districts. The tax is levied on wages, salaries, commissions, net profits or other compensation of people subject to the jurisdiction of the taxing body. Municipalities and school districts levying earned income taxes may exempt people whose income from all sources is less than $5,000 per year from payment of the earned income tax. The exemption must be adopted as part of or an amendment to the tax-levying authority. An earned income and net profits tax for the Pittsburgh School District is authorized by Section 6-652.1 of the Public School Code.

Jurisdictions adopting income taxes under the Local Tax Enabling Act are limited to 1%. Where both the municipality and school district levy the tax, the 1% limit must be shared on a 50-50 basis, unless otherwise agreed to by the taxing bodies.

TAX RATES

There is no statutory limit on the rate Philadelphia may levy for wage and net profits tax. In 1977, a restriction was placed on Philadelphia's power to tax nonresidents.

The Pittsburgh School District tax is limited to 2% as provided by Section 6-652 of the Public School Code. A special provision of the Local Tax Enabling Act allows the Scranton School District to levy the tax at 1% without the sharing requirement mandated for other school districts under Act 511 of 1965.

All other jurisdictions adopting income taxes under the Local Tax Enabling Act are limited to 1%. Where both the municipality and school district levy the tax, the 1% limit must be shared on a 50-50 basis, unless otherwise agreed to by the taxing bodies.

The sharing requirement and the crediting provisions of the act, were intended by the

Legislature to limit the cumulative effect of wage taxes upon a taxpayer. The sharing provisions automatically halve the taxes by overlapping jurisdictions as they apply to residents. School districts may not levy earned income taxes on nonresidents.

Earned income taxes are also subject to the overall limits on taxes enacted under Section 17 of the Local Tax Enabling Act.

TAXABLE INCOME

Section 13 of the Local Tax Enabling Act establishes uniform definitions for earned income, net profits, domicile and other terms. These definitions supersede any omission or contrary definitions in the local tax authority. The definitions are designated as exclusive, and political subdivisions are prohibited from altering or changing them.

Often questions arise as to the inclusion of certain classes of income not directly covered by the definitions in Section 13. Some tax officers have used the regulations issued for the state personal income tax to answer such questions; however, these regulations have no legal status for local earned income taxes. Local taxing bodies may use the state regulations as a guideline in formulating their own regulations, but they must be careful to exclude classes of income taxable under the state personal income tax, but not under the earned income tax. Earned income tax regulations must exempt unreimbursed ordinary and necessary business expenses from the tax base. Under certain circumstances, income from rents or investments can be taxed as net profits of business. Income from Chapter S corporations is not subject to the local earned income tax.

The Pennsylvania Supreme Court has ruled that the tax is levied on total earned income. Taxpayers may deduct business losses from wage and salary income. However, the court let stand a prior Commonwealth Court ruling that taxpayers could not apply net losses from one business against net profits from another. Liability for

earned income taxes on net profits is to be calculated for each business separately under current court rulings. The act specifically includes partnerships as taxpayers for purposes of the local earned income tax.

State law provides for sharing of income tax information between the Internal Revenue Service and the state Department of Revenue. The Department of Revenue also shares tax information with school districts. Districts are authorized to share this information with their constituent municipalities.

Determination of residency is a critical element for earned income taxes. A resident is defined as a taxpayer domiciled within the taxing district.

Determination of residency is a critical element for earned income taxes. School districts may only tax residents of the district; municipalities may tax nonresidents, but must credit liability for their taxes against taxes paid at the place of residence.

A resident is defined as a taxpayer domiciled within the taxing district. Domicile is defined as the place where one lives and has one's permanent home and to which one has the intention of returning whenever absent. Actual residence for a special or limited purpose does not constitute domicile.

When Pennsylvania residents are employed in another state and subject to a state or local income tax at their place of employment, the local taxing body must credit against their liability for local taxes the amount of tax paid out of state. The same dollar of the out-of-state tax cannot be claimed as credit against liability for both state and local taxes in Pennsylvania, but courts have held that the credit can be divided and apportioned against Pennsylvania state and local tax liability. Tax payments made voluntarily to another state do not qualify for the credit, and this credit does not extend to taxes paid to foreign countries.

Section 6913 of the act requires every employer having a factory, workshop, branch, warehouse or other place of business within the taxing jurisdiction to register with the earned income tax officer. All employers are mandated by law to deduct

the earned income tax from their employees whenever the authority of a taxing jurisdiction is listed in the *Earned Income Tax Register* of the Department of Community Affairs. If the ordinance or resolution is not listed in the *Register*, employers are not required to withhold taxes levied under the Local Tax Enabling Act from employee wages.

Responsibility for transmitting withheld taxes of nonresidents to the employees' place of residence rests with the tax officer, not with the employer.

Where the tax authority taxes residents of the district only (school districts), the employer is required to withhold only from resident employees. Any other withholding under a resident-only taxing authority is voluntary on the part of the employer, usually done for the convenience of the employee.

Sometimes called a residence or poll tax, a per capita tax is levied equally on all adult residents or inhabitants of the taxing jurisdiction.

The exception to this rule is the earned income tax levied by the Pittsburgh School District. The district may require withholding of its tax from a nonresident employer who is believed to employ a resident of the district.

PER CAPITA TAXES

A per capita tax is a flat rate levied upon each adult within the taxing district, with no connection to employment, income, voting rights or other factors except residence within the community. Commonly referred to as a "head tax," it is derived from the Latin words, "per," meaning "by," and "capita," meaning "heads." Sometimes called a residence or poll tax, it is levied equally on all adult residents or inhabitants of the taxing jurisdiction.

The tax is authorized in the respective sections of the School Code for second through fourth class school districts. A maximum rate of $5 is authorized. Districts under the authority of the Local Tax Enabling Act may levy an additional per capita tax at a maximum rate of $10. Where a coterminous municipality and school district wish to levy the tax, the maximum rate must be shared between them.

Jurisdictions levying the per capita tax under

authority of these acts are permitted to exempt people whose income from all sources is less than $5,000. The exemption must be adopted by the governing body, which has authority to adopt regulations for processing claims for the exemption. In determining whether or not a married person qualifies for the exemption, the courts have held that the income of the spouse cannot be taken into consideration. The court held the General Assembly had defined those in poverty as people whose income is below the limit, and local jurisdictions cannot distinguish between members of this class based on additional criteria of need or family relationships.

However, Commonwealth Court upheld a municipal per capita tax ordinance limiting the exemption to low income people over age 62 as a reasonable classification. This case upheld application of the per capita tax to indigents, and stipulated the granting of exemptions under the Local Tax Enabling Act or exonerations under the Local Tax Collection Law is a matter of discretion with each individual taxing district.

OCCUPATION TAXES

Historically, the occupation tax was considered to be a tax on property; in this case the property consisted of the office or occupation. It is difficult for modern people to think of an occupation as a form of property. However, remember that when the first taxes on occupations were levied, many offices were created by a grant or letter of appointment and could sometimes be sold or transferred, and that the practice of certain occupations required authorization and/or memberships in guilds or professional associations. Nor does it require much imagination to recognize that many occupations require licensing (doctors, lawyers, engineers, electrical and plumbing contractors, and many others), that membership in a union is often a prerequisite to the practice of certain trades, and that many professions require certain prerequisites even where the law is silent (teachers and professors). Unlike

earlier centuries, such occupations are not transferable by the occupant, and some may choose to call the practice of the occupation or profession a privilege rather than a property right.

However, courts distinguish between occupation and privilege taxes. Occupation taxes are not based on income. "An occupation tax must be identical for all members of a particular occupation whereas a privilege tax is based on some other criteria...." Because they sound alike, occupation taxes are sometimes confused with *occupational privilege taxes.* Commonwealth Court clearly distinguished between these two taxes in a 1971 case. An occupation tax may only be levied on residents and must be measured by the assessed value of a particular occupation. The occupation tax is levied on residents of a taxing jurisdiction regardless of where their occupation is practiced. An *occupational privilege tax* must be levied on residents and nonresidents alike and may only be levied by the jurisdictions in which the occupation is pursued.

The occupation tax may be levied at a flat rate, with a maximum $10 limit, or on a millage applied against the assessed value of occupations.

The occupation tax is authorized by the Local Tax Enabling Act. It may be levied at a flat rate, with a maximum $10 limit, or on a millage applied against the assessed value of occupations. There is no limit on occupation taxes levied on a millage basis under Act 511, and any change in the rate requires reenactment of the tax, following the mandatory publication requirements of Section 4 of Act 511.

This authority has been used by school districts to impose extremely high tax rates to compensate for low valuations and to produce significant tax yields. There are tax rates on record as high as 1,100 mills (110%).

If a school district lying in more than one county levies an occupation tax, it must be levied uniformly on each occupational category existing in each county. If valuations differ between counties, the district must levy on the lowest valuation of any county uniformly throughout the district. School districts and municipalities cannot set their

own occupational valuations; they must use the figures established by the county assessment board.

Jurisdictions levying the occupation tax are authorized to exempt from the tax people whose income from all sources is less than $5,000. The exemption must be adopted as part of or as an amendment to the tax-levy authority. The governing body has authority to adopt regulations for processing claims for the exemption.

ASSESSMENT OF OCCUPATIONS

Whether or not the county levies an occupation tax, county assessors are required by the Assessment Law to list all inhabitants over 18 years of age and value their occupations. Taxing bodies levying occupation or per capita taxes are authorized to provide for preparation of a list of taxpayers by their own employees. Jurisdictions not satisfied that the county assessors have located all taxables may use this authority; however, valuations of occupations set by the county assessment board must be used.

Occupations are usually classified into groups. There are no statutory guidelines as to the number of classifications, or how they are to be made. In some counties all occupations are valued at the same rate.

Occupations are usually classified into groups. There are no statutory guidelines as to the number of classifications, or how they are to be made. In some counties all occupations are valued at the same rate. One county court (Dauphin) upheld assessment of all occupations at $250, stating there is no requirement that occupations be classified and valued by category. However, another county court (Mifflin) invalidated a single uniform assessment as creating a flat rate tax above the statutory $10 limit.

Usually categories reflect to some extent the differential in earning power among occupations, however they do not bear direct relationship to the income of an individual in the category. But economic return is not the sole measure of the value of an occupation. Pennsylvania courts have held that factors other than income affect the value that may be attributed to an occupation.

Values do not have to reflect changes in earnings;

the occupation tax is clearly not an income tax. Neither do classifications have to reflect differences among job types and descriptions within classifications. Clumping related job types in a single classification meets the constitutional test of uniformity, unless the classification is unreasonable.

The courts held a separate classification for retired people over age 65 was not unreasonable, and the court upheld Montgomery County's practice of assessing the value of occupations of full-time students and retired people as "none." The Supreme Court upheld exclusion of minors from the occupational assessment rolls as reasonable. Commonwealth Court ruled that retired people and homemakers do not have taxable occupations and are excluded from the scope of the occupation tax. Occupation taxes cannot be levied upon clergy; to do so would violate First Amendment rights to free exercise of religion.

The occupational privilege tax is the one tax a political subdivision may collect from nonresidents regardless of what other taxes they pay where they live. The current maximum statutory rate is $10, and is subject to sharing between the municipality and the school district.

OCCUPATIONAL PRIVILEGE TAXES

Authorized by the Local Tax Enabling Act, the occupational privilege tax is levied for the privilege of engaging in an occupation within the taxing district. In contrast to the *occupation tax*, from which it is separate and distinct, the occupational privilege tax is levied on residents and nonresidents alike who are employed within the taxing body's jurisdiction.

The occupational privilege tax is the one tax a political subdivision may collect from nonresidents regardless of what other taxes they pay where they live. The current maximum statutory rate is $10, and is subject to sharing between the municipality and the school district.

Section 2 of the Local Tax Enabling Act permits each taxing authority to exempt from its occupational privilege tax any person whose yearly income from all sources is less than $5,000. Taxing bodies are authorized to adopt regulations for processing claims for exemptions.

The location (or situs) for the occupational

privilege tax is the actual place where the individual taxpayer works, not the headquarters of the employer where the payroll checks are prepared. If a taxpayer works in more than one political subdivision during the tax year and is subject to more than one occupational privilege tax, the act establishes priorities of liability. Because the situs of the tax is the place of employment, no taxing district may levy this tax as though it were another kind of per capita tax. It is intended to be a tax only on gainfully employed people. If gainful employment takes people into more than one taxing district levying the tax, priorities of collection are:

- The political subdivision in which the person maintains the principal office or is principally employed
- The political subdivision in which the person resides and works if the political subdivision of residence imposes the tax
- The political subdivision in which a person is employed imposing the tax which is nearest the person's home. The place of employment is to be determined as of the day the taxpayer first becomes subject to the tax during the calendar year. The legislative intent as expressed in the law is that no person is to pay more than $10 in a calendar year for occupational privilege taxes, regardless of the number of political subdivisions levying the tax where the person may be employed during the calendar year. A tax receipt evidencing prior payment must be accepted by all other political subdivisions.

Taxing jurisdictions may require employers to withhold occupational privilege taxes if the tax is listed on the *Register for Earned Income and Occupational Privilege Taxes* maintained by the Department of Community Affairs.

REALTY TRANSFER TAXES*

The realty transfer tax is the only local tax authorized in a law providing for state taxes. Originally authorized separately in Act 511 for local governments, the Local Tax Enabling Act and the Tax

Reform Code now jointly authorize its levy at the maximum rate of 1% on the transfer price of real property within the taxing jurisdiction. If both municipality and school district levy the tax, they must share the 1% maximum. The tax is usually paid by the purchase and affixing of deed transfer stamps to the transfer documents.

The county recorder of deeds is mandated by law to be the collection agent for the realty transfer tax. Local political subdivisions for whom the tax is collected do not compensate the recorder of deeds, but 2% of the amount collected is withheld to reimburse the county for the cost of collection.

Here is the first example of what may happen when the commonwealth imposes a tax that already is in use by political subdivisions. In 1951, the commonwealth imposed a real estate transfer tax at a rate of 1%. The authorizing act contained a specific provision stating it would not invalidate similar taxes then or subsequently imposed by local governments under existing legislation. The Tax Reform Code was amended in 1986 to authorize local taxing bodies to levy realty transfer taxes on the same transactions taxed by the state. The state tax is collected from the purchaser of the property.

Although the Local Tax Enabling Act says nothing as to which party should be liable for the tax, most local ordinances make it payable by the seller. The tax is imposed only on transactions where there is a real transfer of beneficial interest.

Transfers exempt from the tax are listed in Section 2 of the act. They include transfers:

1. By will, mortgage or interstate laws.
2. Trading in residences for newly built residences.
3. To nonprofit housing and industrial development corporations.
4. Between specified family members and family farm corporations.
5. To nonprofit historic, recreational, scenic, agricultural or open space conservancies.

6. For making mortgages or ground rents.
7. For correctional deeds.
8. To the United States or the commonwealth, or any of their instrumentalities, agencies or political subdivisions, by gift, deed or condemnation.
9. To trustees for debt security.
10. In sheriff sales to mortgage holders.

BUSINESS GROSS RECEIPTS TAXES*

*(**Editor's Note:** The use of this source of revenue was limited by the Local Tax Reform Act, 72 P.S. 4750.533. Specifically, the Tax Reform Act repealed authority to levy this tax. The act did contain a "grandfather" clause for those districts that had already enacted the tax prior to Nov. 30, 1988.)*

Business gross receipts taxes are levied upon the privilege of doing business within the jurisdiction. These taxes are variously known as mercantile or business privilege taxes, but are now more commonly referred to as business gross receipts taxes. Despite different names, they are essentially the same tax.

Mercantile taxes on wholesale and retail trade were generally levied first because they are easier to administer. The Local Tax Enabling Act does not define the nature of a mercantile tax, except where Section 8(2) limits the rates imposed on wholesale dealers, retail dealers and restaurants. Mercantile taxes are generally considered as falling into these groups. Business privilege taxes are also levied on the privilege of doing business within a jurisdiction. They are generally of two types: the first applies to all business, except those subject to a mercantile tax; the second is a universal business privilege tax covering all people doing business where the jurisdiction has no separate mercantile tax. The differences between mercantile and business privilege taxes are more semantic than real.

Business gross receipts taxes are measured by the gross receipts of the person doing business.

To be valid, tax liability must be measured by the actual gross receipts. The tax is imposed on the taxpayer, or the person engaged in business without regard to the number of establishments maintained. It is not a tax on separate places of business. Business gross receipts tax ordinances usually exclude political subdivisions, employment for a wage or salary, and businesses where power to tax is withheld by law.

Business gross receipts taxes are levied under the general power to tax people, transactions, occupations or privileges under the authority of the Local Tax Enabling Act.

Business gross receipts taxes are distinct from earned income taxes and occupational privilege taxes. Each is levied on a different tax base with a different group of taxpayers. The privilege of engaging in an occupation is different from the privilege of engaging in a business. For instance, an attorney employed by a company is engaging in an occupation, while an attorney in private practice is engaging in a business as well as an occupation.

Business gross receipts taxes are levied under the general power to tax people, transactions, occupations or privileges under the authority of the Local Tax Enabling Act. The act authorized levy of business gross receipts taxes subject to a limit of one mill on wholesale vendors and one and one-half mills on retail dealers and restaurants. Gross receipts taxes on wholesale and retail businesses and restaurants are subject to sharing provisions when levied by both municipality and school district under the Local Tax Enabling Act.

The School Code authorizes the Pittsburgh School District to levy a mercantile tax, but also includes amusement and recreation businesses and is subject to a rate limit of one-half mill on wholesale business and one mill on retail business.

The imposition of new business gross receipts tax was prohibited after Nov. 30, 1988, under the terms of the Local Tax Reform Act. Even though most of the act remains ineffective because of the failure of the voters to adopt a constitutional amendment in 1989, the court found this prohibition to be in effect. The act also prohibits rates of business gross receipts taxes from being increased

above levels in effect on Nov. 30, 1988, or extended to subjects not taxed as of that date.

AMUSEMENT/ADMISSIONS TAXES

Amusement taxes are levied on the privilege of engaging in an amusement and are measured by admission prices to places of amusement, entertainment or recreation. Admissions taxes are somewhat more general, being levied on admissions to all places or events whether or not they constitute amusements. The Local Tax Enabling Act restricts these taxes to a maximum rate of 10%. When both municipality and school district levy the tax, it is subject to sharing provisions.

A series of court cases have upheld the validity of the amusement tax as a tax on the privilege of engaging in an amusement levied on the patron, as opposed to a tax on the operator of an amusement facility.

Admissions to motion picture theaters may not be taxed. Real property used for camping purposes may not be considered a place of amusement; but admissions to campgrounds have been held taxable where the ordinance levies an admissions tax on all places and events, not just amusements. Amusement or admissions taxes may not be levied on memberships or charges for health, fitness or weight control facilities. The act now establishes the tax base for admissions to ski facilities as 40% of the cost of the lift ticket, for admissions to golf courses as 40% of the greens fees and for bowling alleys as 40% of the cost of admission.

A series of court cases have upheld the validity of the amusement tax as a tax on the privilege of engaging in an amusement levied on the patron, as opposed to a tax on the operator of an amusement facility. However, a municipal taxing ordinance could not require a school district to collect an amusement tax on admissions to football games, absent express statutory consent.

The nature of the amusement to be taxed is not defined in the Local Tax Enabling Act. The definition usually is placed in the tax levy authorization. An admission tax was upheld as applied to a county fair, when the Superior Court found the tax

fell upon the privilege of attending a fair, not upon the fairground itself. In this case, the ordinance levied an admissions tax on a variety of activities not necessarily considered amusements, and specifically included admissions to fairgrounds. The court noted agricultural and horticultural exhibits had less draw for people than the various types of amusements and entertainments offered at the fair.

A taxing body has the right to provide its own set of operative definitions in the tax levy authority. Commonwealth Court upheld application of an amusement tax against admissions to a builders' show in a case where the taxpayer argued it was not commonly understood as an amusement; but the tax ordinance did include trade shows, craft shows and similar exhibitions in the definition of amusement. Such definitions can vary from traditional or customary usage, but not to such an extreme as to render the language senseless.

However, Commonwealth Court found caverns were not a place of amusement within the meaning of the Local Tax Enabling Act or the local ordinance. The caverns were classified as an educational experience of historical, natural and geological dimensions. As opposed to the local ordinance in the *Cambria Township* case where admissions to fairgrounds were specifically taxed, in this case the local ordinances were restricted to admissions to amusements. Also, a museum and fort operated by a foundation for historical and educational purposes was held not to be an amusement within the meaning of the act.

An amusement tax can be considered general in nature, even if it falls only on one enterprise within the taxing jurisdiction. A local admissions tax cannot be applied against a racetrack, according to Commonwealth Court which held the state had preempted the field by virtue of its 15% tax imposed on all admission fees paid by patrons at a thoroughbred racing track. Application of an amusement tax to whitewater rafting operations was upheld, even though the operators pay a license fee to the state. The court held the local tax fell on the

patrons, and not on the operators who pay the state license fee. An amusement tax can be applied against cover charges levied at the door of restaurants and night clubs.

MECHANICAL DEVICES TAXES

Amusement taxes levied against coin-operated mechanical devices have been upheld by the courts. The admission fee was defined as the amount of money required to operate the machine. The tax is restricted to machines providing amusements, including jukeboxes, pinball machines, video games and coin-operated pool tables. The tax can be measured by the gross receipts from such machines, however, it cannot exceed the sum of 10% of each individual price to activate the machine.

OTHER TAXES

The taxes discussed in the previous sections are the principal non-real estate taxes levied by Pennsylvania local governments, either under the general enabling laws or under special laws. They have been widely applied across the state. In addition to these more common taxes, there are a number of current local taxes not widely applied in Pennsylvania. Some have direct statutory authorization limited to one or a few subdivisions. Others are levied under general enabling legislation, but have been adopted by only a few jurisdictions.

PARKING LOT TAXES

Taxes on the gross receipts of commercial parking lots enacted under the authority of the Local Tax Enabling Act have been upheld. In reviewing Johnstown's 10% parking lot tax, the Supreme Court stated: "There can be no doubt of the city's power to enact a tax such as is here under consideration. The Local Tax Enabling Act clearly confers authority for the enactment of such a tax." A 15% parking tax levied by the Moon Area School District fell only on parking facilities close to Greater Pittsburgh International Airport, but the Supreme Court upheld the tax, saying it did not impinge on

interstate commerce and the tax was justified because taxpayers benefited from the existence of a civilized society of which education was a part. However, in a later case the court ruled the district has no power to compel the collection of the tax by an agent of the county under contract to manage county-owned airport parking lots.

Pittsburgh adopted a 10% tax in 1962 on the gross receipts of commercial nonresidential parking operations. The rate was increased to 15% in 1968 and 20% in 1969. The U.S. Supreme Court upheld the tax, holding it did not violate the Due Process clause of the Fifth Amendment nor the 14th Amendment, even though the city parking authority competed directly with the taxpayers. The court held a tax cannot be declared unconstitutional because it renders a business unprofitable. It found the Pittsburgh tax a valid revenue measure.

In 1973, the tax on parking lot operators was replaced by a 20% tax on patrons of nonresidential parking places. This tax was upheld by the Pennsylvania Supreme Court. In 1992, parking taxes were levied by nine municipalities and four school districts.

LANDFILL TAXES

*(**Editor's Note:** Further imposition of landfill privilege taxes has been terminated by the enactment of the Municipal Waste Planning, Recycling and Waste Reduction Act. This act establishes a host municipality benefit fee of $1 per ton to be paid by operators of landfills or resource recovery facilities. The act preempts and supersedes any tax on landfills or resource recovery facilities above the rate in effect on Dec. 31, 1987. No new landfill privilege taxes may be enacted.)*

In past years a few townships and school districts have levied taxes on the operators of landfills under the authority of the Local Tax Enabling Act. In 1981, Smith Twp., Washington Co., levied a 10% tax on the gross receipts of operators of sanitary landfills and chemical, liquid waste or other refuse disposal facilities. Williams Twp., Northamp-

ton Co., adopted a sanitary landfill business privilege tax in 1982 at the rate of 3% of gross receipts. This tax is limited to receipts from landfills operations. In 1983, Carroll Twp., Washington Co., levied a 10% landfill business privilege tax. This does not appear to be limited to sanitary landfills, but extends to every place fill is dumped. Montgomery Area School District, Lycoming Co., levied a landfill dumping privilege tax in 1984 at the rate of 30 cents per tire per vehicle delivering refuse to landfills within the district. In 1992, landfill privilege taxes remained only in seven municipalities and two school districts.

REAL ESTATE OCCUPANCY TAXES

*(**Editor's Note:** Invalidated by a Commonwealth Court ruling in 1987.)*

A number of Allegheny County municipalities levied occupancy taxes under the authority of the Local Tax Enabling Act. In 1971, Forest Hills Borough levied an occupancy tax on all occupants of buildings at the rate of $40 per year. The tax was levied on both owners and renters of residential, commercial and other buildings suitable for human occupancy. In 1978, the rate was raised to $50 per year, payable on a quarterly basis. A similar tax at a rate of $40 per year was levied by Swissvale Borough in 1978. Other taxes ranged from $25 to $50 per year.

These real estate occupancy taxes were struck down by Commonwealth Court in a challenge to the $25 annual tax levied by Crafton in 1987. The court found that such taxes were indistinguishable from per capita taxes. As such, the Crafton tax was invalid because it violated the $10 limit on per capita taxes found in Section 8 of the Local Tax Enabling Act.

RESIDENTIAL CONSTRUCTION TAXES

*(**Editor's Note:** Protests from the building industry, construction unions and financial institutions led the General Assembly to prohibit this tax in 1981.*

All residential construction taxes were prohibited after June 30, 1982.)

In the late 1970s school districts began levying taxes on residential construction, usually imposed on applicants for building permits to construct a residence or convert a building into a residence. The tax was generally a flat rate ranging from $150 to $2,500 or at a percentage of the cost of construction.

The first challenge to this tax was upheld by Commonwealth Court. The court upheld an $875 residential construction tax as a valid privilege tax on the owner's privilege of using realty as a location for a residence. The distinction between newly constructed and already existing residences was upheld as a reasonable classification.

In a second challenge, Commonwealth Court invalidated a tax on the privilege of obtaining a building permit and engaging in building construction. The tax was levied at the rate of 1% of the cost of construction, repair or renovation of any type of building. The court found the tax to be unreasonable and operated with an exclusionary impact against newcomers. The effect of the tax "is to exempt most of the present residents from an added tax, while collecting it mostly from families coming into the community."

SIGN TAX

Emmaus Borough levied a tax on signs under the authority of the Local Tax Enabling Act beginning in 1948. The tax is levied on signs of any nature attached to any building, pole or post or exterior of any structure for purposes of display or advertisement. For signs less than 20 square feet, the tax rate is $5 per year. For larger signs, the rate is $5 per year for every 50 square feet or fraction thereof.

Stroudsburg Borough levies a sign privilege tax on signs located off the premises of the business they are advertising, at the rate of $2 per year per square foot of sign area. Neither of these taxes has been tested in court.

TRAILER TAX

Section 2(8) of the Local Tax Enabling Act prohibits levy of a tax on mobile homes or house trailers subject to real estate taxes unless the same tax is levied on all other real estate within the taxing jurisdiction. A number of school districts had levied house trailer taxes on mobile homes not carried on the assessment roll. These taxes were levied at a flat rate of $2 to $8 monthly and terminated when the mobile home was put on the assessment roll. The tax was principally an interim tax between the time the mobile home was moved into the district and the time it was assessed for real estate taxes.

However, lower court cases invalidated house trailer taxes as levied on mobile homes permanently attached to the land or connected with water, gas, electric or sewage facilities. The courts ruled such mobile homes are subject to real estate taxes, whether or not they are actually on the tax rolls, and are not liable to be taxed under a house trailer tax. These decisions essentially removed the tax base for trailer taxes. By 1992, only three school districts and two townships retained a trailer tax.

LEASE RENTAL TAXES

Middletown Area School District levied a tax on the privilege of renting tax exempt real estate under the authority of the Local Tax Enabling Act. The tax was levied at the rate of 5% of the rental paid by companies and people leasing real estate not appearing on the tax rolls, excluding residential dwellings. In a challenge to this tax, the county court held a company leasing a service station from the Pennsylvania Turnpike Commission was exempt from the tax. The tax would eventually be a burden on the commission, which is exempted by state law from all local taxes. The court raised the question of whether the privilege of leasing tax exempt realty is a proper subject of taxation, but did not address this issue.

Lower Swatara Twp. adopted a similar tax in 1972 at a rate of 5%, but exempted leases from the

Turnpike Commission. The tax was raised to 10% in 1974. The tax chiefly falls upon private firms leasing facilities at Harrisburg International Airport. Benner Twp., Centre Co., also levies a lease rental tax at the rate of 5%. It falls chiefly on individuals and private firms renting tiedowns and hangars at an airfield owned by Penn State University, a tax-exempt entity.

RECREATIONAL USE TAX

A number of small townships in northern Pennsylvania enacted recreational use taxes, usually a flat rate charge levied against structures used for seasonal or recreational purposes. The main burden of the tax falls on owners of hunting and fishing camps in forested areas. Only one such tax was reported in 1992.

* *Indicates the section was excerpted with permission from:* ***Taxation Manual, Sixth Edition,*** *PA Department of Community Affairs, Harrisburg, PA, January 1993.*

State Funding

CALCULATING STATE SUBSIDIES

Pennsylvania's Constitution requires the General Assembly to provide for the maintenance of a "thorough and efficient system of public education," which establishes the basis for state funding of public schools. Funding occurs in a number of separate appropriations in the annual state budget such as: basic instruction, pupil transportation, special education, school construction and vocational education.

A variety of formulas are used to allocate state aid for these purposes among local school entities; however, several factors are frequently used.

• **Aid Ratio** – Many school funding programs are intended to help equalize resources among school districts. Measures of real property and personal income wealth are frequently applied to various subsidy calculations. This market value/ personal income aid ratio is, simply, a means of comparing the theoretical relative wealth of one district to its 500 counterparts across the commonwealth. It is determined by adding 60% of a district's market value ratio and 40% of its personal income ratio. (Some state subsidies, such as those for pupil transportation, school construction and vocational education, use the market value aid ratio only.) Aid ratios are higher for less wealthy districts, lower for those with greater wealth.

• **Average Daily Membership; Weighted Average Daily Membership** – Another key element of many school funding formulas is the number of students enrolled. In some instances, a simple count of all pupils from kindergarten through the 12th grade is used – known as the district's Average Daily Membership. Often, however, a

different method is employed that weights students at the secondary level more than those in the elementary grades. This Weighted Average Daily Membership is computed by multiplying the number of students at the following levels by the indicated weighting factor: half-day kindergarten, .05; full-time kindergarten and elementary, 1.0; and secondary, 1.36.

• **Actual Instructional Expense** – As its name implies, this is the total outlay of a district for the costs typically associated with the daily operations of public schools. AIE includes expenditures such as teacher salaries and benefits, textbooks and building maintenance, to name a few. Often, actual instructional costs are expressed on a per weighted student basis or AIE/WADM.

The General Assembly is charged to provide a "thorough and efficient system of public education," which establishes the basis for state funding of public schools.

• **Equalized Mills** – This is an expression of a school district's local tax effort, determined by dividing the total of all local taxes collected by the district's market value (the State Tax Equalization Board determines the market value). For example, if a district collected $2,199,000 in total local taxes and had $87,960,000 in estimated market value, its local tax effort would be 25 EM: $2,199,000/$87,960,000 = .025 or 25 EM.

• **Base Earned for Reimbursement** – A funding calculation based on instructional costs and local tax effort, using the following formula:

State Median - State Highest EM - S.D. EM
AIE/WADM - (State Highest EM - State Lowest EM x $200)

• **Basic Instruction** – This is the most important state subsidy for public schools. More than $3 billion or the largest single line item appropriation in the entire state budget reimburses school districts for a portion of actual instructional costs. Because this subsidy is so large and serves such a critical role in public school funding, it is frequently revised by the General Assembly.

For many years, this aid was distributed as the Equalized Subsidy for Basic Education, which generally reimbursed districts based on their

weighted pupil counts (WADMs), aid ratios and a fixed amount, known as the Factor for Educational Expense that legislators adjusted from time to time. ESBE included several supplements that assisted targeted groups of school districts, such as those with high incidence of pupils living in poverty or with above average local tax efforts. Another adjunct to the ESBE formula assisted small districts.

In 1993, the subsidy program was extensively changed when the General Assembly initiated a new "foundation" funding system. The revised program essentially freezes ESBE allocations and provides additional state support to ensure that an established dollar amount, or foundation level of funding, is available for the instruction of every public school pupil. Districts' allocations are based on several factors.

- **ESBE** – The total amount of funding actually received by a school district in the 1992-93 fiscal year under the ESBE formula and all of its supplements becomes a base entitlement under the foundation system.
- **Equity Supplement** – Districts with aid ratios of .5000 or greater, and 19.5 or more equalized mills and total pupil expenditures of $6,193 per ADM or less qualify for equity supplement funding. Payments are based on the ADMs and aid ratios of the eligible districts.
- **Poverty Supplement** – Additional funds are paid to school districts that do not qualify for the equity supplement but which have 35% or more of their students in average daily membership whose households receive Aid to Families with Dependent Children. These districts receive $100 for each such student.
- **Foundation Guarantee** – This component establishes a foundation figure per WADM that every district is assured of receiving when adding together its 1992-93 ESBE payment, the equity and poverty supplements (if any) as well as the equivalent of 19.5 mills on estimated market value for total local taxes. (The formula does not mandate that school boards levy taxes at that level; it

simply assumes that amount of local revenues is available for the purpose of this calculation.) If the total of those figures divided by a district's Average Daily Membership is less than the foundation figure, the commonwealth pays the difference as the foundation guarantee.

- **Growth Supplement** – Additional funds are paid to school districts whose pupil populations grew by at least 4.5% or 250 ADMs from 1990-91 to 1991-92. This payment is calculated by multiplying the increase in student population from 1991-92 to 1992-93 times $400 and the district's aid ratio.
- **Additional Supplements** – Any district with an aid ratio in excess of 0.700 that does not qualify for any of the other supplements or guarantees receives special assistance, computed by multiplying $77.50 by its total ADMs. Another allocation was set aside as a discretionary fund for financially distressed school districts.

In 1993, the subsidy program was extensively changed when the General Assembly initiated a new "foundation" funding system. The revised program essentially freezes ESBE allocations and provides additional state support.

These basic instructional funds are paid to school districts six times a year. The first five payments are 15% of the estimated net subsidy and are made on the fourth Thursday of August, October, December, February and April. The balance is payable June 1.

VOCATIONAL EDUCATION

The method of calculating the state's subsidy for vocational education varies slightly depending on whether students attend an area vocational-technical school or an approved vocational curriculum in their home high schools. The basic formula multiplies three factors: the lesser of a district's Actual Instructional Expense per Weighted Average Daily Membership (AIE/WADM) or its Base Earned for Reimbursement; its aid ratio (but not less than .375) and its Vocational Average Daily Membership. This latter figure is adjusted depending on the location of the program. If a student is attending an AVTS, the VADM is multiplied by 0.21; for

a school district-operated vocational curriculum, the factor is 0.17. These adjustments are intended to reflect the added cost of operating vocational programs as compared to offering the regular education curriculum.

Payments are sent six times a year, on the same schedule as basic instructional subsidy funding. Act 117 of 1986 altered the method of payment by sending subsidy funds directly to school districts and vocational schools for the students they educate.

Subsidy payments for vocational education are sent six times a year, on the same schedule as basic instructional subsidy funding.

The amount of state funding for an AVTS is determined by adding the product of these calculations for all sending school districts. This total then is proportionately reduced, if necessary, to bring the allocation in line with the amount appropriated.

PUPIL TRANSPORTATION

Section 2541 of the School Code authorizes reimbursement for school districts that provide transportation for students. Funding is determined by multiplying the Approved Reimbursable Cost by the district's Market Value Aid Ratio: ARC x MVAR = regular reimbursement.

The State Board of Education is responsible for determining the ARC, which is a function of the age and size of the vehicles, the mileage each vehicle travels, how efficiently the vehicle is used, and the "excess" hours required to operate the vehicle under certain conditions. These allowances are increased each year using a cost index that is derived from the Consumer Price Index. The ARC establishes a maximum limit to the funding a district can receive.

In addition to the regular reimbursement, district-owned vehicles receive a depreciation allowance of $700 or 1/10 of the purchase price of the vehicle, whichever is less. That figure, in turn, is subtracted from the vehicle allowance and added to the regular reimbursement.

The School Code also mandates payment of

The State Board of Education is responsible for determining the ARC, which is a function of the age and size of the vehicles, the mileage each vehicle travels, how efficiently the vehicle is used, and the "excess" hours required to operate the vehicle under certain conditions.

"excess costs." To calculate this figure, one-half mill of the district's estimated Market Value is added to the sum of the reimbursement for each of the vehicles serving the district and then subtracted from the total of the district's ARC. The difference is the excess cost: ARC - (1/2 mill MV + reimbursement) = excess cost.

This provision is intended to ensure that no district will need to raise more than one-half mill times its market value to pay the cost of transportation.

A separate appropriation provides additional state aid at the rate of $159 per nonpublic pupil transported. Districts also are guaranteed to receive at least 50% of the allowable costs for transporting nonpublic students as well as pupils residing in hazardous areas.

There are four types of transportation that may be provided by a school district:

- **Contracted Services** – Transportation can be provided through a negotiated contractual agreement between the local school entity and individual parents, bus companies and other administrative units to operate school buses, station wagons and other motor vehicles to transport pupils for a school system. Most pupil transportation is of this type, with the cost negotiated between the local educational agency and the contractor.
- **District-Owned Equipment** – Service also may be operated by the school entity using its own equipment and personnel to transport pupils to and from school, field trips or extracurricular activities.
- **Fare Base** – In some areas, transportation is provided by common carriers over established routes and schedules.
- **Board and Lodging** – Section 1374 of the School Code mandates free transportation for children in special education programs and, when it is not feasible to provide transportation, the board of school directors may pay for suitable

board and lodging. School districts and intermediate units rarely use this method.

Reimbursement to school districts is calculated using the approved allowances (vehicle characteristics, mileage, utilization, excess hours) and the type of service provided (contracted, district-owned, fare-base, board and lodging) multiplied by both the cost index and by the Market Value Aid Ratio. If a school district provides a combination of transportation services, calculating its state reimbursement can become very complicated.

Payments are made according to the following schedule: In August, school districts receive the equivalent of 10% of the transportation subsidy received in the previous school year. Once the district submits data on its prior year costs, it receives an additional 20% within one month. Another 25% payment is made in December to all districts that have submitted current year figures. In March, the state brings districts up to 80% of the projected balance they are owed for the year. The final payment is made in June.

A separate payment of $159 per pupil transported to nonpublic schools is paid to school districts in two installments: 50% in December and 50% in June.

SPECIAL EDUCATION

In 1991, the General Assembly repealed the "excess cost" method of funding programs for exceptional children. In its place, Act 25 of 1991 created a new formula for determining state payments. The revised system consists of several major elements:

• **Payments to School Districts –** The flow of state dollars for special education was dramatically altered. Most of the funds are now sent directly to school districts. (Under the excess cost system, the money went to the provider of service – in most cases, intermediate units.) For the 1993-94 fiscal year, special education allocations are calculated on the basis of the following formula: $1,025 x 15% of ADMs and $12,000 x 1% of ADMs.

Payments are made in six installments: in July, September, November, January and March districts receive 15% of the amount owed, with the balance paid in June. The shift to a formula resulted in a phase-out of most "tuition recovery." Tuition recovery was a procedure which deducted from a district's basic instructional subsidy payment the regular education costs of students in special education.

• **Payments to Intermediate Units** – Five percent of the total state special education appropriation continues to be paid directly to intermediate units as funding for "core services," which are those that support special education programs in the areas. These payments are made in three installments: 50% in August, 45% in November and the remainder in June. In addition, IUs are paid to transport students to special education and early intervention programs. IUs also receive state funding for institutionalized special education programs (see below).

• **Approved Private Schools** – Certain exceptional children exhibit disabilities of such severity or diversity that appropriate educational programs cannot be provided by the public schools. These students may be placed in licensed private schools. A subsidy provides for the tuition and maintenance of children attending such day classes or residential programs. The school district of the student's residence is required to pay 40% of the actual tuition and other costs of maintaining a child in an APS or their own tuition charge, whichever is greater. State payments are made quarterly upon approval.

• **State Schools and Hospitals** – Some children with severe disabilities are placed in state centers and hospitals. Students' home school districts are liable for their own tuition rate or 40% of the per-pupil cost of the state-owned schools, whichever is greater.

• **Early Intervention** – Act 212 of 1990, the Early Intervention Services System Act, mandates that the commonwealth provide services to infants, toddlers and other eligible young children with

disabilities and their families. The lead agency for early intervention services for children from birth to two years of age is the Department of Public Welfare, and PDE is responsible for such services for children below school entry age but above two years. Intermediate units provide screening and referrals. Services are provided by private agencies, school districts and IUs under contract to the appropriate state agency.

• **Instructional Support** – State special education regulations require school districts to provide instructional support in the regular education environment for all elementary students experiencing academic difficulty, including assessment and intervention strategies designed by instructional support teams. State funds are provided to provide training for IST members as well as for hiring instructional support teachers.

• **Institutionalized Children** – On or before the first day of July, every intermediate unit must submit for review to the Pennsylvania Department of Education a report on the actual costs of operating and administering classes or schools for institutionalized children. Following a review of the previous year's annual report, PDE determines the amount of reimbursement owed to IUs by the commonwealth, based on expenditures and available state funds. The districts of residence of institutionalized children reimburse the commonwealth at their tuition rate. Section 1306 of the School Code, as amended by Act 16 of 1993, states that school districts where institutions are located are responsible for providing appropriate services for any child who is suspected or identified as eligible for special education. Section 1309 also permits such districts to collect from districts of residence of such students a special education charge of up to an additional 50% of the regular tuition rate.

• **Contingency Fund** – Two percent of the total special education appropriation is set aside to meet "extraordinary expenses" of special education programs.

INTERMEDIATE UNITS

Act 102 of 1970 established 29 intermediate units, successors to the office of county superintendent, to provide support services to school districts, including but are not limited to: curriculum development, instructional materials and continuing professional development. A state subsidy provides funding for IU administration, programs and services as well as for the lease and purchase of buildings. Funding for such other IU operations as special education, nonpublic school services and transportation are provided under the appropriate state subsidies.

As revised by Act 117 of 1986, most of the state's operating subsidy for IUs is equally divided. The first half is equally apportioned among the 29 IUs; the remaining half is paid on the basis of the ADMs of the school districts comprising each IU.

As revised by Act 117 of 1986, most of the state's operating subsidy for IUs is equally divided. The first half is equally apportioned among the 29 IUs; the remaining half is paid on the basis of the ADMs of the school districts comprising each IU. Additional funds to support IU operations are provided by the participating districts in accordance with the IU's approved budget.

The 1986 law also revised the funding system by permitting IUs to purchase office buildings and warehouse space, but not classroom facilities. Those expenses, as well as lease payments, are eligible for state reimbursement. Payments are based on the approved lease agreement, mortgage or other instrument, adjusted by the IU's computed aid ratio, and are sent to IUs twice a year, in July and December.

SCHOOL CONSTRUCTION

The state's modern role in funding school building projects dates to the 1950s, when "baby boomers" were heading to school in record numbers. As new schools were built, local property taxpayers strained under the relatively sudden financial pressure.

The General Assembly recognized that school districts were not equally able to meet the fiscal burden of such new construction and, in 1956,

established a program of shared responsibility between the commonwealth and local districts for school construction costs. Districts were reimbursed for expenses incurred for new construction, additions or alterations to existing facilities to meet the growing need for more classroom space. State aid was based on the number of pupils served, separate per-pupil reimbursement levels for elementary and secondary facilities, and the district's ability to share in the costs (such as its aid ratio).

In succeeding years, the General Assembly revised the reimbursement formula several times, first to include vocational-technical schools in the program, and second, on several occasions, to update reimbursement levels. The latest adjustment, approved in 1987, established those rates at $3,900 per elementary pupil, $5,100 per secondary pupil, and $6,300 per AVTS/ comprehensive high school pupil. It was the first such change in 20 years. These funds are appropriated in the annual state budget as school rentals and sinking fund payments.

State reimbursement is based on the "rated capacity" of the buildings, with reimbursement made in accordance with the schedule of the district's annual or semi-annual payment on the debt of the bond issue or note.

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RETIREMENT AND SOCIAL SECURITY

The cost of retirement and Social Security for public school personnel is shared by the commonwealth, local school entities and employees. The employee's share of the retirement fund is established by law at 5.25% for those hired prior to July 22, 1983, and 6.25% for all new personnel after that date. The commonwealth and school districts share the remaining costs equally, as determined by the Board of Trustees of the Public School Employes' Retirement System. PSERS uses actuarial calculations to determine the required level of contribution.

School districts and the commonwealth also share responsibility for paying the employer's contribution for Social Security. The amount is calculated on the basis of an employee's salary, the Social Security maximum base for payment, and the contribution rate for a given year.

SCHOOL HEALTH SERVICES

Section 2505.1 of the School Code authorizes reimbursement for school health services according to the following schedule:

Medical Examinations – $1.60 x pupils enrolled with comprehensive health records.
Dental Examinations – $.80 x pupils enrolled with comprehensive health records.
Dental Hygienists – $2 x pupils enrolled (in lieu of subsidy for dental services).
School Nurses – $7 x pupils enrolled. (One nurse may not serve more than 1,500 pupils.)

Act 25 of 1991 revised the funding formula for school health services by providing for separate noncategorical reimbursement. Currently that is computed at the rate of $9.70 times the school district's ADMs.

NONPUBLIC SCHOOLS

Section 923-A (24 P.S. 9-973) of the School Code provides for the acquisition and purchase of textbooks and instructional materials; Section 922.1-A (24 P.S. 9-972.1) provides for auxiliary services. These payments are made as follows:

- **Textbooks** – The number of children enrolled in the nonpublic school on the first day of October of the preceding year multiplied by a minimum of $20 (more, if state funds permit).
- **Instructional Materials** – The number of students enrolled on October 1 of the previous year multiplied by at least $10. This, too, is permitted to increase if sufficient state funds are available. If the appropriated amount does not cover the statutory amount, a reduction fraction is applied.

• **Auxiliary Services** – For services provided by intermediate units, the fully funded amount is derived from pupil enrollment in the nonpublic schools multiplied by at least $72. This amount is subject to changes in the median actual instructional expense per WADM, and a reduction fraction.

OTHER STATE SUBSIDIES

The commonwealth provides funds to school districts for a variety of other programs and services:

• **Driver Education** – Reimbursement is offered at the rate of $35 per pupil completing 36 hours of classroom instruction and six clock hours of actual driving. This aid is paid from the state's Motor License Fund.

• **Homebound Instruction** – State funds are provided for the instruction of children who are confined by temporary illness or injury and who are unable to attend public school. Payments are based on an approved hourly rate ($4/hr.) multiplied by the approved hours of instruction, adjusted by a district's market value aid ratio.

• **School Food Services** – A subsidy provides matching funds on a per-meal basis for schools participating in the National School Lunch, Milk and Breakfast programs. A federal subsidy is paid for each meal served, with an additional amount allocated for meals served to children from low-income families.

• **Education of Disadvantaged** – This program offers state funding for one-half of the 20% local match required for federal funds for programs serving educationally disadvantaged children. The remaining 10% local share may be provided by school districts in the form of in-kind contributions such as rent, lighting and administrative support.

• **Dropout Prevention** – Funds are available to school districts to assist in coordinating the resources of schools with those of employment and social services agencies to enable children to remain in school until they graduate. Program

grants range from $25,000 to $50,000. Federal funds supplement that support.

• **Pregnant/Parenting Teens** – Since 1985, a competitive grant program has been available to assist school districts, vocational-technical schools and intermediate units in initiating programs to assist pregnant teenagers and teenage parents to graduate. Programs must have a minimum of 25 students.

• **Orphans/Foster Children** – Where non-resident, dependent children are placed in private homes by court order and enrolled in the public schools of the receiving district, the commonwealth is responsible for 100% of tuition costs of the district providing the education. Other institutionalized children, such as those in orphan homes and correctional facilities, are educated at the expense of the district where their parents reside. If that is not known, the child is considered a ward of the state and the commonwealth pays the tuition charge.

• **Youth Development Centers** – The commonwealth supports nine centers for children under the jurisdiction of the juvenile courts. Educational programs, including remedial instruction in reading, language arts and mathematics and GED preparation, are provided under contracts with school districts, IUs and private agencies.

• **Migrant Children** – State funds support the operation of classes and transportation for children of migrant farm workers. Usually this is a summer session limited to 40 days. Payments at the rate of $1 a day for each migratory child are made after July 1 of each year.

• **Payments in Lieu of Taxes** – School districts, counties and townships each are reimbursed 20 cents per acre for all state parks and forests, as well as federal forests, which are exempt from taxation. The subsidy also reimburses local governments for property acquired by the commonwealth for flood control or water conservation purposes. Payments are made on or before September 1 of each year.

• **Public Utility Realty Tax Act** – School districts and other local jurisdictions are compensated by the commonwealth for the tax exemption of public utilities. Under the Public Utility Realty Tax Act, the state collects a 30 mill or 3% tax on the book value of all public utility real estate, keeps one half of those revenues for its own use, and distributes the remainder to all local taxing jurisdictions that apply for a share of the money. Funds are allocated among the requesting jurisdictions on the basis of a formula which considers their total local taxes actually collected. Distribution of PURTA funds is unrelated to the presence of public utility in the school districts or municipalities receiving the aid. Requests must be submitted to the Department of Revenue by April 1 of each year.

Chapter 4

Federal Revenue

BASIS OF FEDERAL ROLE

Historically, education has been a federal concern, a state responsibility and a local function. While the U.S. Constitution contains no specific reference to education, national interest in education surfaced as early as the Northwest Ordinance, which was adopted under the original Articles of Confederation. That federal law required certain lands to be set aside for schools. Other early education laws primarily focused on higher education. Later, new states seeking admission to the Union were required by Congress to provide a system of free public education.

Currently, most of the federal funding for elementary and secondary education is concentrated on a few major programs. Federal programs can be divided into two groups. First or primary focus programs include:

- Chapter 1 of the Elementary and Secondary Education Act of 1965.
- Chapter 2, the block grant program (a consolidation of about 30 small programs).
- Impact Aid for federally affected school districts.
- Individuals with Disabilities Education.
- Vocational Education.

A second tier of smaller programs includes the Drug-Free Schools and Communities Program, Bilingual Education, Magnet Schools and the Math-Science Program. A major education-related program is child nutrition (school lunch and breakfast program administered by the U.S. Department of Agriculture).

In addition to programmatic initiatives, the federal role in education increasingly includes a host of social mandates (civil rights, labor standards, asbestos abatement), tax code revisions and other indirect actions affecting schools.

VOCATIONAL EDUCATION

During World War I, the federal government became increasingly involved in educational activities. National interest in vocational education resulted in the enactment of the Smith-Hughes Act of 1917, which began a federal support program for vocational education that continues today. The law extended the study of agriculture, home economics and other industrial subjects to the secondary level.

In response to a growing trend in automation, Congress in 1963 passed a new Vocational Education Act. This program was designed to improve vocational education for people of all ages and to help prepare young people for the workplace of the future. The law also provided funding for consumer and homemaking education, special programs for the disadvantaged and supportive services. Funds, for the most part, were distributed by formula grants.

Resurgence of national interest in education, technological developments, high rates of unemployment, and the gradual shift from an industry-based economy to a service economy prompted Congress in 1990 to pass the Perkins Vocational and Applied Technology Education Act. The funds are to supplement, not replace, state and local funds.

The recent resurgence of national interest in education, coupled with technological developments, high rates of unemployment, and the gradual shift from an industry-based economy to a service economy prompted Congress in 1990 to pass the Perkins Vocational and Applied Technology Education Act. Designed to meet the needs of the current and future workforce, the new law reauthorized the Vocational Education Act with greater emphasis on special need populations, technology and innovations. Federal funds used under the Perkins Act are to supplement, not replace, state and local funds.

Under this new law, public school districts, area vocational-technical schools, intermediate units and eligible post-secondary institutions are entitled to funds for new and expanded vocational

programs. Vocational programs include: cooperative education, industrial arts, along with consumer and homemaker education. These funds cannot be used to maintain existing vocational programs.

The Perkins Act, budgeted at $1.2 billion in 1992, also requires eligible agencies to use the funds to improve vocational education programs with high special needs populations (such as disabled and disadvantaged students). Funds are also allocated on a competitive basis for new tech-prep programs that combine secondary and post-secondary technical education. Pennsylvania currently receives more than $50 million for vocational programs.

SCHOOL LUNCH PROGRAM

Most federal aid to education programs are limited to certain problems deemed national in scope. The National School Lunch Act of 1946 was enacted as a result of widespread incidences of undernourishment and surplus commodities. Public policy to safeguard the health and well-being of the nation's children supports this program's continued assistance to schools in making lunches available to children.

Currently, reimbursements are provided for all lunches, with an additional amount for reduced-price lunches and special assistance for free lunches. The U.S. Department of Agriculture oversees the operation of the school lunch program, as well as school breakfast and milk programs enacted under the Child Nutrition Act of 1966. Pennsylvania currently receives close to $200 million for child nutrition programs.

In recent years, despite federal cutbacks in most social programs, the amount of federal aid for child nutrition programs has kept pace with rising costs and totals more than $6 billion.

IMPACT AID

One of the oldest and most successful examples of federal support is the Impact Aid program, which provides assistance to school districts that are

adversely affected by federal activities. Following World War II, the federal government became aware of the difficulties local education agencies were experiencing as a result of rapidly growing military and defense-industry installations. To compensate districts for the cost of educating children in federally impacted areas, Congress passed P.L. 81-874 that provides aid for school maintenance, and P.L. 81-815 that provides assistance for school construction. More recently, Congress added funding to assist school districts to adjust to military base closings.

Impact aid is a direct federal-to-local program and the money received by school districts can be used as general revenue.

Impact aid is a direct federal-to-local program and the money received by school districts can be used as general revenue. Funding is provided for two categories of children: those who reside on federal property with parents who are employed there; and children who either reside on federal property or have parents employed on it. Congress is expected to significantly revamp this program in coming years. In 1990, 23 Pennsylvania school districts shared more than $3 million in Impact Aid.

NATIONAL DEFENSE EDUCATION ACT

The launch of Sputnik I by the Soviet Union in 1957 was the motivating force for a policy of increased federal involvement in education. For 1959-60, the federal share of elementary and secondary education expenditures was 3.7% nationally and 1.8% in Pennsylvania, according to the Advisory Commission on Intergovernmental Relations. Much of this assistance was categorical aid and funding restricted to a particular purpose.

The goal of the National Defense Education Act of 1958 was to improve the teaching of science, mathematics and foreign languages at all school levels. In later years, some portions of NDEA was incorporated into new education legislation. Currently, this can be seen in the Eisenhower Mathematics and Science Education Act of 1988.

ELEMENTARY AND SECONDARY EDUCATION ACT

Prompted by the civil rights movement of the 1960s, the federal government established equal educational opportunities as public policy. One year after enactment of the Civil Rights Act of 1964, significant federal education legislation was signed into law. Title I of the Elementary and Secondary Education Act provided categorical grants to schools to improve the educational opportunities of disadvantaged children. These funds could be used for a wide range of programs.

The far-reaching provisions of ESEA established the framework for federal aid: target populations, supplementary funds, categorical aid and discretionary funds, and formula and competitive grants.

ESEA included a number of other purposes. Additional "titles" provided funds for libraries and instructional materials (Title II), innovative programs (Title III), research (Title IV), and the strengthening of state education agencies (Title V).

A new Title IV was created in 1974 when Congress revised the law to consolidate a variety of programs, including some from NDEA. However, the merger was not particularly successful as many of the former categorical programs retained their separate identities.

Other categorical aid programs have been added to ESEA since 1974. These programs include Title VI state handicapped education grants (that ultimately became a much larger program – P.L. 94-142), and bilingual education (Title VII). A number of other special programs include: school desegregation, women's education, drug and alcohol abuse, preschool education, ethnic heritage, health, gifted and talented education, environmental education, the arts, and metric education. These were later consolidated in Chapter 2 of ECIA in 1981.

The far-reaching provisions of ESEA established the framework for federal aid: target populations, supplementary funds, categorical aid and discretionary funds, and formula and competitive grants. Unprecedented amounts of federal aid

were channeled into education as a result of the influential legislation.

The federal share of elementary and secondary education expenditures for 1979-80 was 9.2% nationally and 8.5% for Pennsylvania. By 1987-88 it was 6.3% nationally and 5.3% for Pennsylvania. The coming of ESEA also led to vast numbers of regulations and massive amounts of paperwork for school administrators.

Expansion of federal categorical programs with their accompanying regulations and substantial increase in federal funding for education contributed to the creation of the U.S. Department of Education in 1980. Prior to that time, education programs were administered by the Office of Education in the former Department of Health, Education and Welfare.

EDUCATION CONSOLIDATION AND IMPROVEMENT ACT

Sixteen years after ESEA's enactment, landmark federal legislation drastically revised federal funding for education. The Education Consolidation and Improvement Act of 1981 signaled a change in direction on the part of the federal government's expanding role in education. Although the new legislation repealed most of ESEA, it retained many of the principles of the original law. Under ECIA, the largest categorical aid program from ESEA (Title I) continued as Chapter 1 and nearly 30 small categorical education programs were consolidated into one block grant – Chapter 2. Other major programs such as Vocational Education, Impact Aid, Handicapped Education and Bilingual Education were not combined.

What was eliminated was much of the burdensome paperwork and grantsmanship associated with federal programs. In addition, the new law returned more authority to state and local education agencies to establish priorities and to direct federal aid. Along with the decline in federal intervention was a relative decrease in the federal role as contrasted with those of state and local governments.

The basic program framework under ECIA is as follows:

• Chapter 1 provides financial assistance to schools to meet the special needs of educationally deprived children. This program was similar to the original ESEA Title I before the addition of numerous amendments and regulations. Chapter I targets the instructional needs of educationally disadvantaged children from areas with high concentrations of low-income families. As with other federal aid programs, services must supplement, not replace, those normally provided by state and local education agencies. Calculation of aid continues under the old Title I formula for counting eligible students.

ECIA returned more authority to state and local education agencies to establish priorities and to direct federal aid. Along with the decline in federal intervention was a relative decrease in the federal role.

• In 1988 Congress added a concentration grant for districts with high proportions of poor children and a new discretionary grant program – Even Start – for early childhood education. Chapter 1 also requires the continuation of state-administered programs for migrant, disabled, neglected and delinquent children. Federal aid under Chapter 1 totaled nearly $7 billion by 1993, making it the largest of federal education spending. Pennsylvania receives about $300 million for its disadvantaged students.

• Chapter 2 provides block grant funds to local and state education agencies for basic skills development, educational improvement and support, and special projects. Chapter 2 consolidated nearly 30 separate programs. By combining the old programs into a single authorization, local school officials are provided more flexibility to determine priorities. Consolidation also provided greater discretion in using funds. The old method of competitive grants is replaced by local formula grants, and a minimum of 80% of block grants are distributed directly to school districts. Funding for Chapter 2 totaled $435 million for 1993, of which Pennsylvania received $18 million.

• In 1988 Congress revised Chapter 2 and targeted use of funds to seven school improvement

categories: at-risk students; instructional materials; effective schools; professional development, including school board member training; personal excellence; innovative projects; and literacy.

OTHER MAJOR PROGRAMS

To make a free appropriate public education available to all children with disabilities, the federal government provides financial assistance for special education. **The Individuals with Disabilities Education Act** distributes both formula and competitive grants to state and local education agencies for, but not limited to, early childhood assistance, preschool and school programs, resource centers, programs for the deaf-blind, and research. Federal aid for education of children with disabilities totals more than $2 billion for 1993. Pennsylvania receives in excess of $80 million annually.

Under this legislation, a wide variety of educational efforts on behalf of children with disabilities are supported. Each year more than 425,000 children nationwide receive early childhood assistance and, in 1993 some 4.9 million children were provided with educational and diagnostic-evaluative services.

To encourage the establishment of adult education programs, Congress enacted the **Adult Education Act,** designed to expand educational opportunities of educationally disadvantaged adults. The public policy goal of AEA is to enable those who qualify to acquire the basic skills necessary to function in society, to complete secondary school and to benefit from employment-related training. Special emphasis is given to programs of instruction in computational skills and in speaking, reading or writing English.

Basic skills services are provided yearly to approximately 4.2 million undereducated adults nationwide. For the period 1973-84, more than 38,000 of Pennsylvania's students who participated in adult basic education programs received a secondary diploma.

In 1991, Congress revised the adult education program to focus on literacy. Federal funds are distributed to states to initiate adult education through local educational agencies, public or private agencies. Not less than 10% of the state grant may be used for the education of institutionalized adults; not more than 20% may be used for secondary-level programs. The federal legislation provides funds for adult basic education programs on a 75%-25% matching basis.

In 1991, Congress revised the adult education program to focus on literacy. Federal funds are distributed to states to initiate adult education through local educational agencies, public or private agencies.

In 1992, states received a total of $235 million based on their relative share of individuals aged 16 and older without a high school diploma.

According to the 1990 census, more than 21% of Pennsylvanians 25 years of age and older lack a high school diploma. In addition, 2.6 million of the commonwealth's general adult population do not have the skills or knowledge necessary to cope with the demands of daily living, according to the Pennsylvania Department of Education.

Since 1965, **Head Start** has served approximately 15 million children from low-income families. Administered by the U.S. Department of Health and Human Services, Head Start provides health, educational, nutritional, social and other services to economically disadvantaged preschool children. In 1993, more than 700,000 children were enrolled in full-year, summer and experimental programs. Pennsylvania receives in excess of $100 million for Head Start.

Schools and agencies offering Head Start are required to provide 20% of the total cost of the program, although this may be waived under certain conditions. At least 90% of the children enrolled in Head Start must come from families whose income is below the poverty level, and at least 10% of the total enrollment opportunities must be made available to disabled children. In recent years, federal aid for Head Start has grown to more than $3 billion.

CHANGING FEDERAL ROLE

Federal aid is available to school districts through myriad programs and various agencies. In addition to the aforementioned programs, funds are provided for other programs, such as bilingual education under the Department of Education, Indian education under the Department of Interior, and energy conservation under the Department of Energy.

As the federal financial role has decreased relative to state and local funding, Congress expanded the number of mandates that impact on local school operations.

As the federal financial role has decreased relative to state and local funding, Congress expanded the number of mandates that impact on local school operations. Indeed, many of those (such as asbestos abatement, the Fair Labor Standards Act, Immigration Law and EEOC requirements) are unrelated to programs of the U.S. Department of Education and, usually, are not accompanied by federal funding to assist in their implementation.

In the early 1990s, the federal government asserted a strong interest in the overall quality of general education, promoting state and local school reform to achieve the National Education Goals.

Chapter 5

Accounting In School Districts

OVERVIEW OF THE ACCOUNTING SYSTEM

Pennsylvania has established a mandatory accounting system to be used by all local education agencies (school districts, area vocational-technical schools and intermediate units). Though structured, the system allows flexibility for local information and reporting needs. The accounting system is based on Generally Accepted Accounting Principles for local government units. GAAP are intended to work in conjunction with state and federal laws.

Standardized accounting provides for uniformity and consistency in recording and reporting financial information. Consistency and uniformity are necessary for LEA financial reports that are the basis for subsidy calculation and evaluation of financial conditions. The system was adopted in 1984 to:

- Provide a method for LEAs to make full disclosure of financial information.
- Provide uniform and consistent information between LEAs by using a standard chart of accounts.
- Provide more reliable financial information for program evaluation and budgetary planning.
- Assure that LEA financial statements are consistent with accounting standards and acceptable to public investors, governmental units, the Legislature, educational and research organizations.
- Comply with federal standards set by the U.S. Department of Education.

Accounting entries may be made in one of three different ways – cash, modified accrual and full accrual. Cash accounting is similar to the process individuals use for maintaining a checkbook; full accrual is used by businesses; governments rely on modified accrual. The distinction is the difference between when revenues and expenditures are recognized. In a cash system, recognition occurs when cash is received or a bill is paid. Accrual recognition occurs when cash is earned or a liability for payment occurs.

Standardized accounting provides for uniformity and consistency in recording and reporting financial information. Consistency and uniformity are necessary for LEA financial reports that are the basis for subsidy calculation and evaluation of financial conditions.

The difference between full and modified accrual is the recording of revenue. Modified accrual records some revenue when cash is received and some when cash is earned. For example, real estate tax revenue is recorded when the bills are issued, earned income tax revenue is recorded when cash is received. Under GAAP standards, the distinction is the ability to accurately measure and reasonably expect payments. GAAP standards also allow current period resources (revenues) to be matched with current period uses (expenditures).

The school accounting system, in addition to GAAP, requires that the general fund budget be prepared on a modified accrual accounting basis. As part of the requirements, reporting of the budget is to be on a change in fund balance format.

ACCOUNTING AND REPORTING STANDARDS FOR LEAs

Governmental accounting standards for LEAs require LEA accounting systems to be organized on a fund basis. Funds available for use by LEAs include:

- Governmental funds – through which most LEA functions are typically financed. Governmental funds include: the general fund, special revenue funds, capital project funds, and debt service funds.
- Proprietary funds – used to account for LEA

activities similar to business operations. The focus of these funds is on income determination. Proprietary funds include: enterprise funds (such as food service operations and child care facilities) and internal service funds (such as self-insurance programs and other service programs provided the LEA by the LEA).

- Fiduciary funds – used to account for the assets held by the LEA as trustee or agent. Fiduciary funds include: expendable and nonexpendable trust funds, and agency funds (such as student activity funds).

Two account groups must also be maintained to account and report the LEAs governmental fund and expendable trust fund fixed assets and long-term liabilities, such as unmatured debt outstanding, capital lease obligations and accrued compensation absence liabilities.

School boards should establish local policy on the appropriate size of the fund balance. A fund balance is as important to an LEA as a savings account is to an individual.

LEAs should establish and maintain only the funds needed for sound financial administration and compliance with School Code requirements. All necessary funds and the two required account groups must be presented in the LEA's General Purpose Financial Statements – a minimum generally accepted reporting requirement.

LEAs must use the modified accrual basis of accounting for all transactions reported in governmental funds, expendable trust funds and agency funds. LEAs are required to use the full accrual basis of accounting for all transactions reported in proprietary funds and nonexpendable trust funds. The cash basis of accounting is not an acceptable basis of accounting for LEA reporting purposes.

FUND BALANCE

A fund balance under GAAP standards is the difference between assets and liabilities for the fund. Assets include cash on hand (cash and investments) plus money due to the LEA. Liabilities include all of the LEA's unpaid bills, payroll and related

deductions, and cash received but not earned. Because assets include unreceived cash, not all of the reported fund balance is available for use, or equivalent to cash.

Because conditions change, the fund balance will also change (increase or decrease). School boards should establish local policy on the appropriate size of the fund balance. A fund balance is as important to an LEA as a savings account is to an individual. An adequate fund balance is important to:

- Adjust to the loss of a major taxpayer/ employer.
- Finance needed facility improvements without borrowing.
- Purchase needed equipment (such as text books) without borrowing.
- Deal with the uneven pattern of cash flow.
- Finance uninsured emergencies and unbudgeted contingencies.

IMPORTANT ELEMENTS OF THE ACCOUNTING SYSTEM

The PDE comptroller's office has prepared a manual that provides the standard coding system for recording LEA financial transactions. The *Manual of Accounting and Related Financial Procedures for Pennsylvania School Systems (Revised)* explains the required accounting standards, funds and classification criteria required to be used by LEAs.

It provides the detail of codes and definitions necessary to comply with PDE reporting requirements. Account codes are shown in three primary groups – revenue, expenditures, balance sheet. Within these three groups are nine required elements (called dimensions) plus several identified local option elements. The manual provides the following explanation of dimensions for revenue and expenditures, along with the appropriate coding structure.

REVENUE DIMENSIONS

Revenues are classified as local, state and federal or other financing sources. Local revenues include money produced within the LEA's boundaries and available for LEA use, and amounts received by another government or entity on behalf of the LEA.

State revenues include money received from the commonwealth. Federal revenues include money received from the federal government for use by LEAs to operate grant programs, either directly or through PDE.

Other financing sources are not considered revenues of the LEA but serve to increase its assets and fund balance. Other financing sources include proceeds from extended term financing, receipts from other funds within the LEA, refund of prior year expenditures, and similar transactions.

Revenues and other financing sources must be reported by fund and revenue function. There is also an option in the school accounting system to record revenues by fund, revenue function, and funding source codes.

- Fund (use required for state reporting purposes) is a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources. It also contains all related liabilities and residual equities or balances, or changes therein.

- Revenue source (use required for state reporting purposes) permits segregation of revenues by source. The primary classification differentiates local, state and federal revenue sources. The category of other financing sources is included in the dimension breakdown, although in a strict accounting sense it is not a revenue. (See revenue section of manual for a more detailed explanation.)

- Funding source is an optional dimension with the revenue classification and, in most instances, would only be used in a revenue account

number structure by those LEAs that are computerized. (See expenditure dimensions for more detail.)

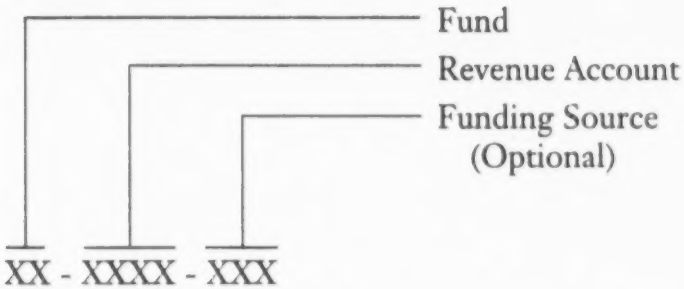
REVENUE CODING EXAMPLE

General Fund Revenue From Current Real Estate Taxes

Fund	Revenue Source
10	6111
Code	**Description**
10	General Fund
6	Local Revenue
1	Taxes Levied
1	Real Estate Taxes
1	Current Real Estate Taxes

CHART 1

REVENUE DIMENSIONS



EXPENDITURE DIMENSIONS

Expenditures are classified as instructional; support; noninstructional; and facilities acquisition, construction and improvement services. Other payments are classified as other financing uses.

- **Instructional expenditures** include activities dealing directly with the interaction between teachers and students, and related costs directly attributable to an instructional program.

- **Support expenditures** include services which provide administrative, technical and logistical support to facilitate and enhance programs of instruction.

• **Noninstructional service expenditures** include activities concerned with providing noninstructional services to students, such as testing and diagnostic services.

• **Facilities acquisition, construction and improvement services** include all capital expenditures (fixed assets) incurred to purchase land, build or renovate buildings, improve or replace service systems and built-in equipment, improve sites, and planning costs.

• **Other financing uses** include all other LEA expenditures not classified above, such as debt repayments, and transfers to other funds within the LEA.

Expenditures and other financing uses must be reported by fund, function, object, funding source and instructional organization. In addition to these required codes, there is an option available to record expenditures by operational unit, subject matter, job classification and special cost center.

• **Fund** (use required for state reporting purposes). *See Revenue Dimensions (p.69).*

• **Function** (use required for state reporting purposes) describes the activity for which a service or material is acquired. The functions of an LEA are classified into five broad areas: instruction; support services; operation of noninstructional services; facilities acquisition, construction and improvement services; and other financing uses.

Functions consist of activities which have somewhat the same general operational objectives. For example, the subfunctions (the first major subdivision of a function) of support services consist of such areas as transportation, pupil personnel services, administration, etc. Instruction subfunctions are by program (regular, special, vocational, etc.).

Design of the functional coding structure at levels below the subfunction classification is based on the principal that the classification of activities

should be related activities that can be grouped and all such classifications are mutually exclusive. Reporting to the commonwealth will generally be to the subfunction level (second digit of the four digit function code); however there may be some reporting that will require using the third digit of the function code.

• **Object** (use required for state reporting purposes) is the service or commodity bought. The accounting manual identifies nine major object categories: personnel services salaries, personnel services-employee benefits, purchased professional and technical services, purchased property services, other purchased services, supplies, property, other objects, and other financing uses.

• **Funding source** (use required for state reporting purposes) permits LEAs to accumulate expenditures to meet a variety of specialized reporting requirements at local, state and federal levels. The first two digits of this dimension identify the funding source (local, state, federal), authority (Title I, Title II), or expenditure purpose (Child Nutrition Projects) for which a special record or report of revenues, expenditures or both is required. The third digit of this three-digit dimensional code is available to identify particular projects (Part A of a Title I project).

• **Instructional organization** (dimension is required for state reporting purposes) segregates expenditures by organizational level (elementary, secondary, etc.).

• **Operational unit** (optional) segregates costs by building structure.

• **Subject matter** (optional) describes a group of related subjects and allows the accumulation of costs for providing instruction for particular subject areas.

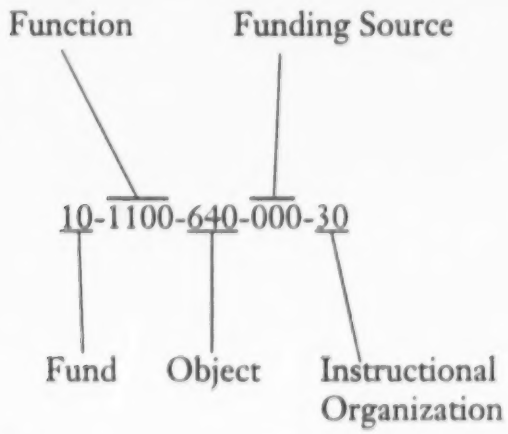
• **Job classification** (optional) enables LEAs to categorize in more detail the job classifications

identified in the Object dimension. This dimension should only be used with the 100 and 200 object codes.

• **Special cost center** (optional) is used by LEAs for classifying expenditures in any other manner needed. Some examples of possible uses are the classification of costs by term, work, order, bus route, building, etc.

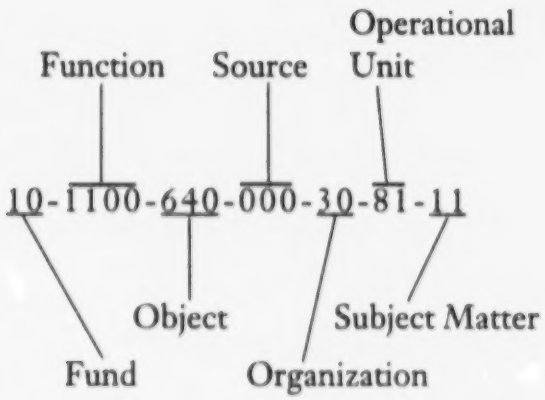
EXPENDITURE CODING EXAMPLE (Required Reporting Dimensions).

The purchase of textbooks used for regular instruction at the secondary education level.



Code	Description
10	General Fund
1100	Instruction - Regular Programs
640	Supplies - Books and Periodicals
000	Noncategorical
30	Secondary Level

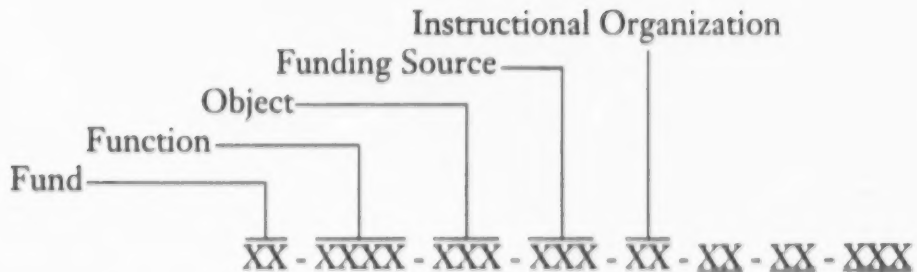
An LEA may decide to use optional dimensions to further classify the transaction. The operational unit dimension may be used if the LEA wanted to know the building where books were to be used. An LEA may also choose to use the subject matter dimension to classify purchases by subject area. The transaction would be coded as follows:



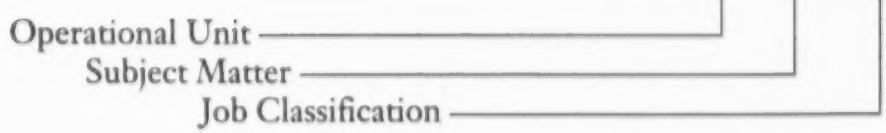
Code	Description
10	General Fund
1100	Instruction - Regular Programs
640	Supplies - Books and Periodicals
000	Noncategorical
30	Secondary Level
81	George Washington Senior High School
11	Mathematics

CHART 2
EXPENDITURE DIMENSIONS

Required –



Optional –



Special Cost Center number of digits varies

X = Digital coding
Fund, Function, Object, etc. = Dimensions

BALANCE SHEET DIMENSIONS

Use of the balance sheet is required for state reporting purposes. The balance sheet account dimension consists of asset, liability and equity accounts. When presented together in a financial statement, the accounts form the balance sheet, the basic financial statement used to disclose an LEA's financial position at a specified date.

BALANCE SHEET CODING EXAMPLE

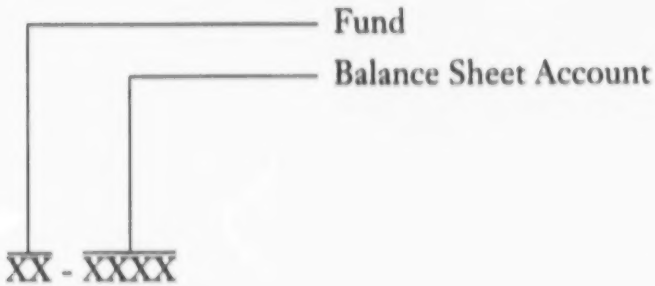
Recording cash in the bank for the General Fund

Fund	Balance Sheet Account
10	0101

Code	Description
10	General Fund
0101	Current Asset - Cash

There is considerable flexibility provided in the accounting manual to allow LEAs to accumulate financial transactions in a manner meaningful for decision makers. Comparability between LEAs exist because of the standardization of the accounting system. However, because of flexibility in the system, comparisons must be approached with caution. Each LEA needs to understand the management philosophy of cost accumulation to make program cost comparisons possible.

CHART 3
BALANCE SHEET DIMENSIONS



82

Financial Management and Planning

Daily activities of controlling and coordinating the use of resources is termed financial management. An organization's financial management activities may be assigned to one or several individuals, but each part of financial management is a distinct activity. School district financial activities are typically the responsibility of the business manager.

While the business manager is responsible for daily financial operations, some functions are performed outside the business office, such as auditing, and tax collecting by elected collectors. Some districts contract payroll processing; others contract risk-management programs. However, the business manager coordinates all these activities.

School district financial management is centered around the district's budget, which is structured according to the chart of accounts. The accounting system is the mechanism to record and report all the financial activities of the organization. Traditionally, each activity of financial management is viewed as a discrete entity. In practice, financial management is the coordination of all financial activities. These activities include:

School district financial management is centered around the district's budget, which is structured according to the chart of accounts. The accounting system is the mechanism to record and report all the financial activities of the organization.

- Budgeting • Purchasing
- Accounting • Payroll
- Auditing • Debt Management
- Tax Collection • Risk and Insurance
- Cash Management (includes banking and investments)

Chapter 6

FINANCIAL PLAN

Traditionally budgets are viewed as a financial plan for school districts. However, a budget is only one part of a good financial plan. As a planning document, the budget is the operating plan for a single year, and for the one year, reflects the price tag to implement activities to accomplish the stated goals of the district.

Financial planning, in its truest sense, is a multiple-year process; oftentimes referred to as a five-year plan. The five-year plan establishes goals and objectives for the district for five years beyond the budget, and becomes the roadmap for the district's travel toward stated goals. The budget is the part of the plan that will be traveled during the coming year. Each year, the first year of the plan becomes the budget and a new plan year is added.

One of the major frustrations of financial planning is that the financial plan never appears to be accomplished. In part, this occurs because of changes in staff, board membership and available resources. A plan is, however, just a plan.

The budget plan is based on assumptions about economic conditions. Other assumptions should include: enrollments, class size, contractual obligations and workforce size. Assumptions used to develop the budget should be clearly stated. As the district progresses on its roadmap toward stated goals, side trips are sometimes added and detours are inevitable. Budget plans should adapt to change.

Side trips and detours occur because funds are limited. Unexpected side trips include changes in enrollments; detours occur because the public may not be willing to contribute necessary resources. Oftentimes, a good objective included in the plan will appear unwise when it comes time to spend dollars. Almost all side trips and detours are the result of changes in public interest and support for education. Other reasons include state regulations, economic conditions and student needs. The role of the annual budget is to translate the roadmap of educational objectives into tangible dollars

(tax dollars) that can be understood and accepted by the public.

Because many programs and services compete for available funds, clear goals and objectives often become lost in the process. One way to keep the destination in view is to set priorities. Thus, effective planning can reduce the need to debate trivial issues. Setting priorities allows the board and administrative staff to focus their talents on the key issues.

WHY PLAN

Planning is the starting point in the board's policy function to provide "thorough and efficient" educational programs with limited resources.

Dan Tollett, executive director of the Tennessee School Boards Association, and Patsy Carriott, a Kingsport City (TN) board member, enumerated six reasons for school boards to plan.

1. Planning is the process by which a school board exercises leadership. School board members can have the greatest impact on a school system through planned change. While it may not be difficult to initiate changes in the system, wise board members realize that changes that are accepted, that last and that are not threatening are those that have been made with forethought and careful planning. Rapid change will have an impact on the system, but generally a negative one. Careful planning and communication will enable a board to move toward its goals with efficiency and support.

2. If a board knows where it wants to go, it is more likely to get there. A carefully developed written plan increases the probability of success. Boards too often find themselves operating with no clear idea of what they want to accomplish. With effective planning, they not only know where they are going, but have carefully developed strategies to help them get there.

3. The educational program a community makes available to its children is far too important to be left to chance. The quality of the educational program provided to the children is the paramount responsibility of the board. Boards should and must be accountable for what happens in the system.

Having a well-conceived plan for the educational program and the means for implementing it takes the chance out of what happens in the system. Responsibility and accountability become the rule rather than the exception.

When a board follows a well-conceived plan, the community perceives that the schools are operated in a businesslike manner. Public support and excitement can result.

4. Maximum use of a community's resources is possible only through long-range planning. While each community's resources are variable and unique, it is only through planning that effective use can occur. Tapping those resources should be neither a random nor sporadic effort, but should be an integral part of the overall planning process. Failure to use valuable community assets may cost the school system in an economic way, and will definitely cost it in terms of community support. When a board follows a well-conceived plan, the community perceives that the schools are operated in a businesslike manner. Public support and excitement can result.

5. Effective planning allows a board to develop and maintain a continuity of purpose. Once a board has established its goals, it greatly diminishes the natural tendency to move in innumerable directions at the same time. The board has a clear idea of its goal, a timetable for implementation and reaffirms on a routine basis its continuing efforts toward the stated purpose. Continuity is maintained regardless of changes in administration or membership of the board.

6. Adoption of a long-range plan is conducive to board unity. The process of developing a long-range plan provides board members an opportunity to share their expectations and priorities for the school district with other members. It

helps the board define differences among members and through compromise leads to group commitment to goals and objectives. A commitment to the same goals and objectives will result in a more cohesive and more effective board.

Boards who plan effectively seem to provide quality programs with less cost and effort. This certainly is a better use of board talent and time and is in keeping with the legislative responsibility given to local school boards.

LEADING THE PROCESS

Good planning involves everyone in the organization. However, planning should have one or two leaders. The characteristics of these leaders should include the following:

- **Inquisitive** – an active learner, who is curious about business, the profession and the world, will take the initiative to get at cause and effect. An avid questioner and listener with a quick, wide-ranging mind.
- **Conceptually uninhibited** – imaginative, bold and a nonconformist in thinking who looks for new ideas or new ways to apply old ones, and has intellectual power to grasp and sort implications and concepts quickly. Speaks his or her mind but reacts well to others' ideas.
- **Competitive** – enjoys intellectual competition and is at times purposefully argumentative to test the strength of others' positions. Looks for strength and weakness in ideas and wins debates without alienating people.
- **Practical** – realistic in judgment, is analytical and objective about what can be done, how fast and with what resources. Logic and manner are persuasive.
- **Tolerant** – able to cope with criticism and rejection; realizes that people are slow to change, but attempts to persevere through the use of logic and reason.
- **Multidisciplined** – knowledgeable in several fields and keeps current with developments in many related fields.

These characteristics are not easily found in any or all people and are not necessarily the bottom line in planning, but they should be sought and identified in those expected to lead in the planning function. Although such people may not be in key positions in a school district's present structure, they can be used in the vital function of planning.

USING A COMMITTEE

Committees can be used effectively to look at the "big picture" and establish a gameplan for meeting identified needs. Financial planning is a process to be used by all individuals or committees, while there may be a specific assignment to a committee for planning in general. Such a committee should save the board members many hours, and also result in a better plan using the special talents that exist on each board.

A planning committee should represent the characteristics stated earlier. This committee should identify activities that impact on financial and program matters in the district. They should use special subcommittees and staff for developing needs, information and assessment procedures.

A written description of the task and established guidelines should be given to everyone involved. The chair of the committee should have an established procedure for reporting to the board and administrative team.

The committee should have secretarial assistance to ensure proper recordkeeping. Records must be accurate and understandable to all involved. The records and reporting are necessary for the plan to evolve and be useful.

A stringent time schedule helps reduce trivia and improve timeliness of information and implementation. When completed, the plan or budget should be presented to the board and the public in a clear, concise manner with emphasis on public understanding and perception. Included as part of the overall plan should be an implementation schedule. Written policy is recommended to aid implementation.

BENEFITS OF PLANNING

Educational leaders must recognize that planning is deciding in the present what to do in the future. Planning comprises the determination of a desired future and the steps necessary to bring it about. It is the process where school districts match resources with their objectives and opportunities as part of the budget process.

School districts that do little multiple-year planning tend to miss opportunities within their resources. As a result, these districts are most susceptible to being affected by the changing times, shifts in perceptions and outside pressures.

Planning encourages systematic forethought by educational leaders. It leads to a better coordination of district efforts. Planning supports development of performance standards, permitting accountability. Using performance standards, the district can sharpen its guiding objectives and written policies. Planning results in preparation for vs. reaction to sudden new developments.

When completed, the plan or budget should be presented to the board and the public in a clear, concise manner with emphasis on public understanding and perception. Included as part of the overall plan should be an implementation schedule. Written policy is recommended to aid implementation.

REALISTIC EXPECTATIONS

Improved preparation still requires realistic expectations. When getting involved in the planning effort, school districts must avoid some common pitfalls.

Some districts see planning as an effort to know the future as if through a crystal ball. The future really is unknowable. These districts fail to understand that planning is an integrated way of determining impact on the future resources. The planning process requires flexibility to take advantage of opportunities. Adjustments must be made to actual events; plans according to written policy must be monitored and updated.

Some school districts go into planning expecting a "cure-all" for school problems. To ensure success, they place their most valued specialist in charge of the plan. Unfortunately, specific

expertise in a speciality area does not guarantee success in the planning function. These people should be involved in the planning process, but not necessarily in leadership roles.

One of the most difficult pitfalls to avoid is "shooting the messenger" who bears bad news. Business tends to reward the person who first brings truthful bad news. Planning should identify both opportunities and problems. It should also establish a time frame for changes in action or implementing plans. Planning cannot solve problems, but it can focus the board's efforts on the problems and opportunities.

The planning process requires flexibility to take advantage of opportunities. Adjustments must be made to actual events; plans according to written policy must be monitored and updated.

KEEPING ON TARGET

Following is a simple checklist for keeping financial planning on target.

- **Stay flexible.** Conditions and situations change regardless of planning.
- **Maintain a balanced outlook.** Don't over-react; keep moving on a timely basis.
- **Get the entire management team involved.** Success depends on everyone having valuable input and identifying with the plan.
- **Be critical of assumptions and forecasts.** Data lend themselves to interpretation and are only as good as the mind that interprets them.
- **Multiple-year budgets** rather than one-year budgets. View the big picture by temporarily washing out the day-to-day operations.
- **Get everyone involved** and commitment will follow. The developed plan must have something for everyone involved in the process.

Planning is not a stepchild of school district organization, but a vital part of the educational management process.

Chapter 7

The Budget

Adopting a budget is one of the most important functions of the school board. Simply stated, a budget is the description of programs and services with price tags attached to achieve stated goals and objectives. A school district budget, no matter how large or small, is a delicate balance of policy choices. The framework surrounding these choices is the extent to which the public will understand and support the choices through taxes.

A school district budget, no matter how large or small, is a delicate balance of policy choices. The framework surrounding these choices is the extent to which the public will understand and support the choices through taxes.

Budgets provide school boards with the opportunity to directly influence the educational environment of the district. Adoption of the budget provides administrative staff with direction and guidance to act. Almost every major decision made by the school board is incorporated into the budget.

Ability to influence the budget also carries a two-part responsibility. First is to provide every child in the district with the best possible educational opportunities. Second is to maximize the use of available resources. Developing a budget requires defining the revenue necessary to support expenditures. Expenditures are defined as program choices for serving students. Revenue choices represent taxpayer impact. Expenditure choices affect employees, students and parents. Revenue choices affect taxpayers, businesses, parents, employees and students. Budget policy will impact everyone both now and into the future.

A BUDGET IS NOT . . .

School boards, along with the administrative team,

are the individuals with insight about all the variables that result in a budget. Therefore, it is the responsibility of the board and administrative team to balance competing demands and produce an educational plan beneficial to the community.

A budget cannot be a partisan political tool and represent the educational needs of the total community. It cannot be self-serving to special interest groups and represent the greater public good. Budget choices are not a forum for achieving personal advantage. A budget should not be the sole basis for evaluating administrative performance. Finally, it cannot be used as a vehicle to censure previous actions.

AUTHORITY

The Pennsylvania Public School Code of 1949 *(future reference to the Pennsylvania Public School Code of 1949 shall be by section number)*, as amended, gives local boards the authority to conduct the financial affairs of the district. The School Code contains provisions that are:

- **Mandatory** – The board must perform certain acts.
- **Permissive** – The board may exercise its discretion and either act, or refrain from acting.
- **Prohibited** – The board may not act, either in total or until certain conditions have been satisfied.

School directors in Pennsylvania generally have more flexibility to raise and spend public monies than in any other state. At least 19 states have requirements for voter approval of budgets or taxes or both. Additionally, at least 12 states require voter approval for capital construction.

Section 687 provides that in districts of the second, third and fourth class the board must:

• Prepare a proposed budget at least 30 days prior to adoption of the budget for the following fiscal year on forms furnished by the Department of Education.

• Make the proposed budget available for public inspection at least 20 days prior to the date set for adoption.

• Provide 10 days public notice prior to any final action on the budget.

• Adopt the budget and necessary appropriations required to put it into effect at a public meeting and file a copy with the Department of Education.

Section 687 also:

• Prohibits deficit financing; the total amount of such budget shall not exceed the amount of funds, including the proposed annual tax levy and state appropriation, available to the district.

• Allows the transfer of any unencumbered balances, or any portion thereof, from one budget category to another, during the last nine months of the fiscal year, or to meet debt service requirements due to State Public School Building Authority.

• Allows the board to change the budget to meet emergencies such as epidemics, floods, fires or other catastrophes, the funds therefore shall be provided from unexpended balances in existing appropriations, from unappropriated revenue, if any, or from temporary loans.

Section 609 provides:

• Districts may receive and expend state and federal funds for specific purposes whether or not they were included in the budget. Districts have used this to increase budgets after adoption to receive and expend state and federal funds.

BUDGET POLICY

Authority is available through board policy. Policy is a function of the board of school directors granted through the School Code and clearly established under the state constitution. Boards are extensions of the Legislature with the responsibility to provide efficient and responsive local control of community schools.

Policies are plans that address identified needs by providing stated purposes, delegated responsibilities and guidelines for desired action. They are written

plans developed by identifying needs, considering alternative solutions, devising a plan of action and evaluation.

Policy clearly is a part of the budgeting process. It should be quite evident that Policy setting is planning and planning, to be effective, must result in written school district policy. Adopted policies should be monitored by the board for accountability. No one policy will cover the entire financial plan. Typically, policies will cover the various aspects of budget preparation and fiscal procedures.

Policy clearly is a part of the budgeting process. Policy setting is planning and planning, to be effective, must result in written school district policy. Adopted policies should be monitored by the board for accountability.

Policy statements should be designed to:

1. Link educational programs and services with the purely financial matters in the district.
2. Establish a set of standards for measuring the district's progress.
3. Fix responsibility to require the district to operate effectively and efficiently.
4. Help establish and maintain a smooth working relationship between the board and the superintendent and among board members.
5. Demonstrate to the public that the board is businesslike in its operations.
6. Help the board maintain leadership and control.
7. Provide stability, continuity and a historical record.
8. Orient new board members and administrators to the district's fiscal management style.
9. Help a board make financial decisions consistent with past ones in situations with similar circumstances.

Some topics that may be covered by policies *(see Exhibit 1, p.132)* include:

- Objectives
- Budget planning
- Budget preparation
- Budget hearing
- Fund balance
- Tax levy
- Purchases subject to bid
- Purchases budgeted
- Purchases not budgeted
- Cooperative purchasing
- Payroll authorization
- Payroll deductions

- Tax collection • Payment of claims
- Tuition income • Petty cash
- Bank accounts • Special purpose funds
- Investments • Shared programs/services
- District audit – public

MORE BENEFITS OF BUDGETS

A budget, if properly prepared and presented, will provide benefits beyond legal compliance. Budget documents can serve as an effective public relations tool. Information presented in such a document can provide ready reference for other processes and actions.

Budget documents should contain information to be used to educate the public. Some more frequently prepared information includes:

- Cost of programs on a per-student basis.
- Where the money comes from. Note that a large portion comes from the state.
- Relationship of costs with programs.
- Costs associated with building maintenance by building.
- Communicate financial need to the business community.

Budget documents contain information for board members and the public about other processes. The related processes include:

- Authority to make expenditures and sets limits on the expenditures.
- Serves as an overview of the educational system in the district.
- Educates the staff about the interrelationship of specific activities.
- Aids in evaluating planned changes and the progress toward completion.

When the budget document includes a multiple-year projection, this provides:

- Public and business community confidence.
- It demonstrates and supports orderly planning and action.

- Establishes a framework for work programs.
- Helps communicate the need for return on the investment of tax resources.

Additional guidelines are available from either Government Finance Officers Association or Association of School Business Officers. Both organizations operate programs designed to recognize excellence in budgeting. These programs set the standard for budget presentation.

Communications and public relations aspects of the budget are important. Information needs to be provided in terms that are concrete, not the abstract totals. Most individuals will never earn in a lifetime what most districts spend in a single year. As such, explanation of an expenditure with, "its only $100,000," is not within the individual frame of reference. What the public does understand is the cost per pupil or the average teacher salary.

Communications and public relations aspects of the budget are important. Information needs to be provided in terms that are concrete, not the abstract totals.

ROLES IN BUDGET PREPARATION

Because the district budget is public policy, everyone has a role in its development. However, all the roles are different, ranging from comment to decision making. Some participants will need the "how to" details; others will only need the policy options supported by good information.

Establishing clearly defined roles is difficult. The complex nature of today's society along with the quantity and quality of information often blur the boundaries of various roles. Because complex relationships are created by the budget process, the cornerstone of appropriate roles and boundaries is public trust and confidence. Budgeting requires a bond of public trust and confidence among board members, the administration team and the public.

BOARD MEMBERS

Most board members agree they don't need to know the "how to" details of budgeting. However,

they need to know priorities, have good information, and be able to question effects and impacts of recommendations. For board members, confidence in the process may be more important than knowing how to budget.

Confidence in the budget process relies upon both established budget policy and the mutually agreed upon budget philosophy. Budget philosophy is about "deciding how to decide." This is the basic framework for budget decision making. Some examples of "deciding how to decide" include:

- Spend money to save money?
- Trade labor peace for controversy?
- Willing to change, or is the status quo untouchable?
- Is the school a business or a public service?
- Will the district cooperate with others or is it autonomous?

How can a school board member, who usually is not a professional educator or financial expert, meet these responsibilities as an elected, unpaid, part-time volunteer?

Confidence in the budget process relies upon both established budget policy and the mutually agreed upon budget philosophy. Budget philosophy is about "deciding how to decide."

First, by relying on the district administration – superintendent, business manager and other management staff – to direct the day-to-day activities, implement new programs, and provide supervision of and control over all resources. Second, by asking for recommendations in areas where the board lacks expertise. Third, by asking questions as necessary to understand concepts and details. Fourth, by comparing proposals to previous budgets. Outcomes of the previous budget plans are then compared to actual outcomes. Fifth, by knowing and understanding, as a board, the goals and priorities of the district, and making sure they are included in the budget.

SUPERINTENDENT'S ROLE

The superintendent, as chief executive officer of the school district and a commissioned officer of the state, must provide information, leadership

and direction to budgeting in the same manner as any planning function. His or her responsibility is to provide these ingredients to assist the board of school directors in dealing with effective financial planning and local responsiveness to community needs.

Superintendents should recommend policy. A recommendation should be based upon familiarity with the day-to-day operations, knowledge of school law and educational expertise. Boards, as well as individuals, will make sound decisions if good understandable information is provided. This then becomes the key role of the superintendent in developing the budget into an effective educational program.

A superintendent must assist the board to develop a budget system, which should be based on the idea that every program or service offered by the school district can be identified and evaluated.

A superintendent must assist the board to develop a budget system, which should be based on the idea that every program or service offered by the school district can be identified and evaluated. Evaluation must be based on the importance of achieving established goals. Whether a program is instructional (English, reading, math) or noninstructional, it should be assessed on the basis of its importance in the education of children.

Importance of a program can be established as follows:

- **Level I:** The program is mandatory or explicitly required to meet a state mandate. It is essential to the proper functioning of another program which is required. Level I also includes those programs that are essential to the health, welfare and safety of students or staff.
- **Level II:** The program is established by local board policy because it meets some clearly articulated local need. This program recognizes a unique and important community characteristic.
- **Level III:** The program is not required, but is desirable. It may enhance the total program; provide diverse exploratory or enrichment opportunities defined by unique local interest.

Superintendents must recognize that resources are limited, and will ebb and flow according to

public support and understanding.

Bottom line – the superintendent's role is to help the board meet the challenge of providing quality programs with limited resources.

CHIEF BUSINESS OFFICIAL

Chief business officials will wear many hats during the course of a day. They are managers of district resources and information, and are the source of timely, accurate and understandable data. Chief business officials are responsible for monitoring the flow of resources necessary to accomplish the board's policies.

Business officials should have the ability to effectively communicate the "bottom line" in an easily understood manner. An effective business official should work closely with the superintendent to assist with all aspects of planning. No one can have too much information if it is formatted for clear understanding in the decision-making process.

Adoption of a budget is considered to be the end of the process. However, the adoption is the midpoint in the budget cycle, as well as the beginning of the next cycle and the ending of the prior cycle.

BUDGET CYCLE AND TIMELINES

Adoption of a budget is considered to be the end of the process. However, the adoption is the midpoint in the budget cycle, as well as the beginning of the next cycle and the ending of the prior cycle.

Budget cycles contain five parts, each centering on a specific activity. While most of the attention is aimed at adoption, this is actually the shortest time span. The five parts are:

- Planning
- Preparation
- Adoption
- Implementation
- Evaluation

In each part of the budget cycle, the focus is a single year. Linkage between years and cycles is often seen only during the **planning** stage when needs are identified and priorities are established.

Typically, this stage consists of about two to five months. Second is the **preparation** stage when information about levels of service, enrollment projections, cost estimates and revenue projections are developed. Time requirements in this part of the cycle vary depending upon the effort expended during planning and the adequacy of the accounting system. **Adoption** takes about one month. This stage includes introduction, public comment, advertising and the actual vote. The typical comment after the budget is adopted is, "Glad that's over for another year." Adoption is not the end of the process, rather it activates the implementation and monitoring phase. This part of the cycle lasts for the life of the budget (one year in Pennsylvania). Following the end of the budget year is the last part of the budget cycle – evaluation – that lasts approximately three months. The relationship between evaluation and the budget process is unclear because of distance (time), and is commonly known as the audit.

Time and overlap of budget cycles often presents confusion. Time periods shown will vary according to the particular budget approach and size of district during the first two parts of the process, but all districts have the same time frames during the last three parts of the cycle.

EXHIBIT 1
BUDGET TIME LINES

Budget Year	1	2	3
Planning	Nov -Mar	Nov -Mar	Nov -Mar
Preparation	Apr -May	Apr -May	Apr -May
Adoption	June	June	June
Execution	July -June	July -June	July -June
Evaluation	July -Oct	July -Oct	July -Oct

EXHIBIT 2
EXAMPLE OF BUDGET CYCLE OVERLAP

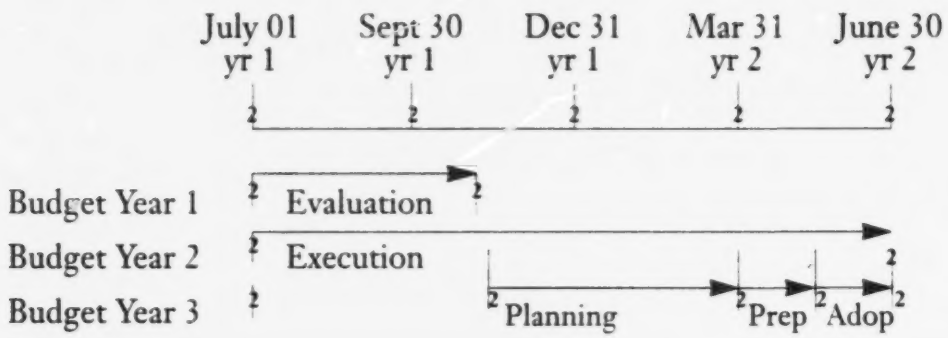


Exhibit 1 shows the time period of three successive budget cycles. Exhibit 2 shows the time period July 1, Year 1, to June 30, Year 2. While this is the implementation phase of the Year 2 budget cycle, this period also contains parts of the Year 1 and Year 3 budget cycles.

A number of budget dates are specified by law. These include: adoption by, public comment period, start and end of the fiscal period (budget year) and completion of audit requirements. The board has authority to establish additional requirements for budgeting. This can be done by local policy. Boards, for example, establish dates for administration status reports, along with summaries of requests. Following is a sample budget timeline.

July-December: Develop budget objectives for coming year by soliciting input from faculty, department heads, building principals, etc.

January-March: Central office constructs first draft of proposed budget.

March-April: Board deliberations regarding budget occur.

May: Adopt preliminary budget early in month.

May 15: Public hearing on a budget. (Public hearings, as such, are not required by the School Code. Section 687 says, in part, "nothing in this act shall be construed to prevent any school district . . . from holding a public hearing.")

May 30: Adopt final budget.

July 1: Mail tax notices.

October 31: Annual Financial Reports submitted to state.

Many boards, as a matter of courtesy, custom and good sound public relations, prepare a formal budget presentation for the public, answer questions and acknowledge concerns. Some districts allow public participation and observation as the budget is debated, assembled and rearranged during the spring months.

PREPARATION OF THE BUDGET

Much of the budget preparation process takes place prior to the board's first review of the budget. Among the preparations should be an appraisal of the past. Did revenue meet projections? Did any budgeting area overspend? Does policy satisfactorily direct budgeting? What other actions or events are learning experiences for future budget consideration?

Preparation should also include projections of the future. What are enrollment trends? At what rate are fixed costs escalating? What are the projected demographics in the district? These are only a few examples of items for consideration when developing a budget.

Look to the administrative team members for appraisal and initial recommendations. They have been closely monitoring district activities on a daily basis. They also have been kept informed on state and federal mandates as well as speculation on funding.

The management team and the board should develop budget objectives well in advance of constructing the proposed budget. Some districts approach the budget process by using one or more of these strategies:

- Subcommittees such as buildings and grounds, curriculum, personnel and finance, to set separate objectives.
- Meeting as a committee of the whole to discuss specific topics for budget planning purposes –

personnel, finance, buildings and grounds, athletic programs, transportation, curriculum, etc. – with or without a subcommittee system.

• Establishing citizens' advisory committees for curriculum, transportation, school closings, etc.

• Developing a five-year plan of action, incorporating one or more of the previous methods, including but not limited to the following:

- Personnel – staffing, negotiations, contracted services.
- Building usage – school closings, construction, remodeling.
- Curriculum – additions, deletions, revisions.
- Transportation – hazardous routes, non-public service, shuttle service, etc.
- Finance – tax assessments, interest rates, tax anticipation notes, debt service.

These strategies should then be the basis for developing the budget. Coordinating the above actions with the district's goals and objectives should improve projections of the future. The process will identify needed additions, deletions and alternatives in personnel, inventory, services, maintenance, transportation and revenue.

As the budget begins to develop, don't start with cost on every item. Begin by satisfying needs, goals and objectives. As ideas are contributed, the tentative budget will gel showing priorities. Costs and revenues should be added after needs are identified. List specific reasons for reducing or postponing other items.

ADOPTING THE BUDGET

A year's effort reaches culmination with the approval of a final budget document. The tentative budget has been open to public scrutiny; additional comments and input have come from various sources and it is now time for adoption.

Section 508 stipulates that a majority of all the members of the board of school directors in every district, duly recorded (roll call), showing how each

member voted, shall be required in order to take action on a number of subjects including adopting the annual budget and levying and assessing taxes.

Failure to have five affirmative votes renders action of the board void and unenforceable. Failing to adopt a budget by July 1 causes the district to lose authority to expend funds.

Remember when adopting a budget, its purpose is to provide children in the district with the best possible educational program maximizing the resources available. Be sure to have had adequate participation in the process, and get sufficient public and staff comment. Develop a clear understanding of every major part of the budget – it is an operating tool – and have sufficient policy to support and direct it. Contingencies are necessary for the unexpected *(see Exhibit 1, p.132)*.

Remember when adopting a budget, its purpose is to provide children in the district with the best possible educational program maximizing the resources available.

BUDGET EXECUTION

Budget execution involves continuous monitoring of revenue and expenditures. Monthly reports are prepared to allow the board to examine progress against the plan. Be conservative when estimating budget revenues and liberal when projecting expenditures.

Monthly reports allow the board to determine if the degree of conservative estimation of revenues and liberal projection of expenditures is appropriate.

Examination of expenditures in any given accounting period will show a number of one-time expenditures. Many one-time expenditures include: insurances for buildings and vehicles, debt service payment of principal, etc. Among the more difficult tasks for a board is to understand which payments are one time and which are continuous. Expending 99% of the budget in the first month is not a problem for an item which is an annual payment. If 99% has been expended in the first eight months for a multiple-payment item, it could signal a problem.

Boards are required to take action on two specific items that directly impact the budget: approve

the payment of bills, and approve transfers. Transfers can only occur during the last nine months of the fiscal period, except for the specific authority of Section 609 relative to state and federal funds (sections 6-609 and 6-687).

Transfers represent changes in resource allocation. These changes may be required to meet unusual conditions or a shift in policy. Other times, transfers may reflect a different way of implementing policy.

While transfers are a normal part of the budget process, caution must be used when changes to the budget are made. Typically transfers are viewed as movement of money between items. A transfer is the shift of resources that could have an impact on programs. Because boards are free to set policy, they also can change policy. A radical change in policy which significantly alters programs may involve sunk costs, staff disruption, waste and inefficiency.

Administering the budget involves hundreds of transactions and an equally large group of documents. Care should be taken by board members not to get involved in details.

As the fiscal year progresses, the board approves contracts, purchases and reacts to public input or changing conditions by altering or setting policy. Understanding the relationship between these actions and the budget is necessary to effectively monitor the budget.

Administering the budget involves hundreds of transactions and an equally large group of documents. Care should be taken by board members not to get involved in details; the role of the board is policy setting, not accounting. Getting drawn into the detail can create disorder.

Remember, budget execution is the implementation of policy, which can occur in different ways. Adjustments to the budget via transfers or differences between budgeted and actual can be the effect of improved implementation.

Auditing, the final phase of the budget cycle, is reviewed in Chapter 8.

Chapter 8

Audits and Auditors

Nothing in school finance is more misunderstood than audits. While there is a generally recognized requirement for review of financial transactions, the purpose and use of audits and related reports is vague.

All school districts are required to have an annual audit. In school districts of the first class, the audit is to be conducted by the city comptroller; all other districts must have their audits completed by a certified public accountant. Selection and payment of auditors is the responsibility of the district.

An audit is the evaluation of the financial condition of a school district – the final grade for the year.

An audit is the evaluation of the financial condition of a school district – the final grade for the year. Examination of the various records of the district are referred to as audit tests, which can be viewed as being similar to tests given to the district's students.

In addition to the district's audit, Section 2553 of the School Code requires the comptroller of the Department of Education to perform regular audits and field audits and may, at his or her discretion, perform special audits to verify allocations of receipts and expenditures. Such audits are usually limited to specific use of program funds given for state and federal projects.

The state Fiscal Code requires the auditor general's office to audit the accounts and records of all school districts. Examination is made by the auditor general of receipts and expenditures related to state payments for public education, is to verify that the monies received from the commonwealth were properly paid and that the district

complied with all laws and regulations. Audit reports, listing discrepancies, will be furnished to the school district.

Activity funds warrant special consideration. The Bureau of School Audits of the auditor general's office has published guidelines for auditing activity funds. Their objectives are to ensure that:

- Basic internal controls are established for effective management of the organization.
- All cash intended for the organization is received, promptly deposited, properly recorded, reconciled and kept under adequate security.
- Cash is disbursed only upon proper authorization, for valid purposes, and are properly recorded.
- Purchases and accounts payable are supported by appropriate documentation, promptly paid and properly recorded.
- Inventory is appropriately safeguarded and properly recorded.

No matter how satisfied district officials may be with the performance of the auditor, it is advisable to limit the consecutive length of time an auditor is with the district.

SELECTION OF AUDITORS

Districts, except those of the first class, can select their own auditors. An important aspect of auditor-client relationship is the degree of independence of the auditor or firm. Independence of the auditor implies that the relationship is limited to performance of audit work to provide an impartial opinion of the accuracy.

One method of maintaining independence of an auditor is to periodically change auditors. No matter how satisfied district officials may be with the performance of the auditor, it is advisable to limit the consecutive length of time an auditor is with the district. A number of different periods or approaches are used to limit an auditor's employment. Typically the length of employment is five or six years, and changing auditors requires finding a replacement. Length of service by an auditor is local choice. One method that is successfully used in the public sector is through a Request for Proposal.

REQUEST FOR PROPOSALS

An RFP for selection of auditors is common practice. While each RFP will meet the unique needs of the district, most RFPs for audit services include:

- A description of the district.
- Length of contract and option for extension or renewal.
- Types of activities to be audited, such as:
  - Tax collector.
  - Bank records.
  - Number and type of funds.
- Reports to be required:
  - Audit report.
  - Management report.
  - Any special reports (such as AFR).
- Time for completion of audit.
- Technical assistance required or necessary.
- A list of current or previous clients for reference.
- Any special conditions or needs of the district not addressed above.

Once the RFP is prepared, the selection process becomes similar to competitive bidding.

DIFFERENT TYPES OF AUDITS

There are three types of audits: financial, performance and fraud. RFPs are generally used for either the financial or performance audit. Fraud audits generally only occur if conditions indicate a need and are an expansion of the other two types.

Financial audits are an examination of the books and records of the accounting system. Performance audits examine the financial records plus the delivery of services in accordance with specific contracts. Performance audits are also referred to as compliance audits. An intermediate unit or a votech might have performance audits to ensure that terms and conditions of service delivery for various school districts comply with contract requirements.

Fraud audits occur only if the other two types of audits indicate missing funds or supplies. Fraud audits are the most detailed and time consuming of

the three types. The scope of a fraud audit is determined by the extent of missing funds or supplies.

PURPOSE OF AUDITS

Except for fraud audits, audits are designed to measure the accuracy of the records maintained by the district. Also integral to the audit is a review of internal controls. Audits are designed to determine if the reports fairly and accurately reflect the financial condition of the district.

Internal control review is designed to ensure that there are reasonable safeguards to protect the resources of the district. Internal controls are those activities designed to minimize the loss of resources. Examples of internal control are: two signatures required on all checks and approval of bills for payment required.

AUDIT REPORTS

Annual audit reports contain several important statements. All statements should be prepared in accordance with generally accepted accounting principles. GAAP represents a standard that has been developed to ensure consistency.

Among the important statements are the balance sheet, and the statement of revenues, expenditures and fund balances. All statements are relative to a point, typically the last day of the fiscal year. Statements by themselves provide information but are more useful when examined for changes between years.

Audit reports also contain a statement of actual compared to budget. Comparison of actual versus budget is intended to show the spending outcome compared to planned.

Another important aspect of the annual audit report is the section titled "notes to the financial statements." Notes are used to explain significant items. Oftentimes, notes will provide detail to support entries on the various statements, and will also show significant weaknesses that may be uncovered.

The auditor's opinion is important for both internal and external use. Opinions are either unqualified, which means there were no problems identified to cause major concern, or qualified. A qualified opinion will cite the reason for the limited qualified opinion. Reasons for such action could be as major as no records or as minor as using cash accounting.

Another report generally issued in conjunction with the audit report is the "management letter." Management letters contain findings which may or may not be significant but represent the potential for future problems; findings focus on internal control. Weaknesses cited in the management letter, like deficiencies cited in audit reports, should be corrected as soon as possible to provide necessary fiscal safeguards.

Completion of the audit and issuance of the audit report and management letter mark the end of the budget cycle for a single year. Audit and management letter findings should be addressed as appropriate, and corrective action should be taken as quickly as possible. Unresolved audit findings can create future problems.

Chapter 9

Fiscal Administration

Fiscal administration involves a number of topics that can be divided into two groups – roles and duties, and activities. Many times the duties and activities are accomplished by one individual. Even though they may be consolidated, it is helpful to understand fiscal administration by examining these elements individually.

ROLES AND DUTIES

CHIEF BUSINESS OFFICIAL

In addition to the duties specified for budgeting, chief school business officials are a key to daily fiscal administration. They are responsible for oversight, coordination and control of daily financial activities. While budgeting is a major component, other areas are cash management, monitoring of revenue and expenditures, ensuring the timely payment of bills, purchasing, and inventory control. Oftentimes this position is integrated with the duties of the school district secretary and/or the treasurer.

SCHOOL DISTRICT TREASURER

Section 404 of the School Code defines the role of the treasurer. The treasurer may be any corporation qualified and legally authorized to transact a fiduciary business in the commonwealth. Board members in districts of the third and fourth class may serve as board treasurer, but not in districts of the second class. The treasurer may also be the business manager.

The treasurer is elected by the board in May of each year for a one-year term beginning July 1.

Section 436: The position must be bonded by a surety bond; the bond shall be provided annually; duties cannot be assumed until bond has been posted.

Section 409: It is lawful for the board to pay for the cost of the bond.

Section 438: School treasurers shall be paid such compensation as the board of school directors may determine; however, second, third and fourth class districts' compensation cannot exceed 2% of the funds paid out on school orders.

Section 440: The treasurer of each school district shall deposit the funds belonging to the school district in the school depository; submit a report monthly to the school controller; submit a report monthly to the school secretary; and make all deposits in the name of the school district. This is often done by the business manager or the business office.

Section 441: The school treasurer shall settle his accounts annually with the board of school directors for each school year.

Section 659: The treasurer shall be furnished with the necessary stationery and books required to perform the duties of the office.

SCHOOL DISTRICT SECRETARY

The School Code defines the minimum duties of the secretary's position:

Section 404: Permits the board secretary to be a member of the board in third and fourth class districts, but not in districts of the second class. Board secretaries are elected to the board in May for a four-year term beginning on July 1 (1993, 1997, etc.). Pursuant to case law, the secretary's election is an appointment. Election is by the board, not the public.

Section 431: A performance bond, in an amount required by the board of directors, is required. It is lawful for the board to pay for the cost of the bond.

Section 434: Every board of school directors may, by resolution, appoint an assistant secretary who shall, in the absence or disability of the secretary, perform the duties and exercise the powers of the secretary. The assistant secretary may be appointed from the membership of the board of school directors, but shall not be any other officer thereof, shall not receive compensation for such services and shall be bonded.

Section 432: The board may decide to pay its secretary in an amount to be determined by the board on an annual basis.

Section 433: The secretary shall keep a correct and proper record of all proceedings of the board; prepare and sign an order on the treasurer for the payment of bills upon the approval of the directors (often done by the business manager); attest, in writing, to the execution of all deeds, contracts, reports, and other instruments that are to be executed by the board; prepare reports concerning the district, on such forms and in such manner as required by the State Board of Education or the secretary of education; generally supervise all business affairs of the school district, subject to the instructions and direction of the board of school directors; be custodian of all records, papers, office property and official seal of the district; keep correct accounts with each tax collector; submit statement of the finances of the board at each regular meeting, which statement shall be entered into the minutes; and perform other duties as required by this act or the board of school directors may require.

FINANCIAL ACTIVITIES

PAYING BILLS

The most visible component of fiscal administration is paying the bills. Sections 439 and 607 of the School Code provide direction for how to process payments. Section 439 provides:

- All bills are to be approved by the board.

- An order "to pay" must be signed by the board president.
- Certain bills may be paid prior to board approval. The conditions for this include: receipt of a discount, avoids a late charge, or other advantages accrue to the district.

Section 607 requires:

- Proper school orders must be drawn prior to payment.
- There must be sufficient funds in the treasury.
- A separate order shall be drawn for each account or payment.

Boards should establish a formal policy for payment prior to approval. Procedures should include specific criteria, and designate the person(s) who may approve such payments.

School orders for payment must contain the budget account upon which the order is drawn. Boards may establish policy regarding process and procedures for the disbursement of funds.

BIDDING AND PURCHASING

School boards are required to purchase and provide all furniture, equipment, textbooks, school supplies and other items for the use of the district. Act 30 of 1990 set a requirement for competitive bidding at $10,000 or more. However, any purchase of $4,000 but less than $10,000 requires three price quotes.

Purchases of $10,000 or more require:

- Public notice by advertisement once a week for three weeks in not less than two general circulation newspapers. If no such paper exists, then the district shall post notices in at least five public places.
- Boards shall accept the lowest responsible bid (where kind, quality and material are equal).
- Boards may reject any and all bids.
- Boards may select a single item from any bid.

Purchases may be made through intergovernmental cooperative agreements (joint purchase agreements) or may "piggy-back" state or other government contracts following the appropriate legal requirements. Even though purchasing may require competitive bidding, boards may establish reasonable criteria such as color, units/size, or any other reasonable criteria specific to the district's needs.

The School Code provides for the exemption of several items from competitive bids. The exceptions include but are not limited to: globes, maps, textbooks, educational films and teacher demonstration devices.

The School Code provides for the exemption of several items from competitive bids. including but not limited to, globes, maps, textbooks, educational films and teacher demonstration devices.

Services are excluded from the competitive bidding requirements. However, certain services are from time-to-time subject to legal challenges. When considering the purchase of services, the legal status should be reviewed with the district's legal counsel.

While the School Code provides for the exclusion of services and certain other items from bidding, school districts may choose to bid those items.

SALE AND DISPOSITION OF PROPERTY

School district property that is considered as district personal property (equipment and inventory) may be disposed of as the district deems appropriate. Boards should set policy to guide the disposition of no-longer needed equipment.

Sale of land and buildings is clearly established in the School Code (Section 707, et seq.).

CASH MANAGEMENT AND INVESTMENT

Cash management is concerned with the receipt of revenue and payment of expenditures. Like an individual, revenues never match expenditures, resulting in periods of extra cash or shortages of cash to meet current expenditures. Another element of cash management is how best to address the periods of excess cash. This is the function of investments.

Investment decisions are generally based on interest rates and payment needs. The calculation of available cash for investment is called cash flow analysis. Cash flow analysis estimates the amount of revenue to be received with demands for cash (bills and payroll). The surplus is then available for investment.

Boards should establish an investment policy to guide where and in what manner investments should be made. If such a policy does not exist, the board will need to approve each investment.

Investments generate revenue to most districts through interest earnings. In some districts, interest earnings generate revenue equivalent to between 1 and 10 mills of real estate tax. That is, without interest income, the district would need between 1 and 10 mills of additional tax revenue.

Boards should establish an investment policy to guide where and in what manner investments should be made. If such a policy does not exist, the board will need to approve each investment.

Investment opportunities are regulated by the provisions of Section 440.1. Investments must be made in:

- Treasury bills or other instruments of the U.S. government.
- Savings accounts, certificates of deposit or other bank instruments insured by either FDIC or FSLIC.
- Instruments of secured deposits backed by the state government.
- Collateral pool (Act 72) or 120% if secured individually.

Other material concerns of cash management include the frequency of deposits and the safe keeping of cash prior to deposit.

TAX COLLECTION AND COLLECTORS

As described in Chapter 2, part of the revenue to fund the budget comes from local taxes. To collect such revenue, the tax must be properly authorized and an individual (or company) must be designated to receive such payments.

Levy of real estate taxes requires an annual authorization. The individual authorized to collect real estate taxes is the elected municipal tax collector (city treasurer in third class, second class and first class cities.)

Act 511 taxes need only be levied once or when the rate is changed. Act 511 taxes may be collected by the individual designated by the board.

Compensation for the elected tax collector may be set by the board. Compensation may be set as either a percent of collection, a fee per tax bill or a flat annual rate.

Compensation for the elected tax collector may be set by the board. However, it may not be set so low as to prevent individuals from seeking office. Compensation must be set prior to the first day to file petitions for election. (Every four years in 1993, 1997, 2001, etc.). Compensation may be set as either a percent of collection, a fee per tax bill or a flat annual rate. Once set, the rate of compensation is fixed for the term of election. If a vacancy occurs, the rate can be changed prior to appointment of a replacement.

Act 511 tax collectors serve at the pleasure of the board of school directors. Appointment as the Act 511 tax collector can be made at any time and compensation can be set accordingly.

*(**Editor's Note:** For more detail on the duties and responsibilities, the reader may request a free copy of the publication: **Tax Collectors Manual:** Pennsylvania Department of Community Affairs Press Office, P.O. Box 155, Harrisburg, PA 17120.)*

BONDING

Prior to taking office, several individuals are required to have surety bonds. Those positions requiring bonds are: secretary of the board, treasurer, tax collectors, individuals responsible for or having authority over cash and bank accounts, including student funds. The board may establish the amount of the bond required (usually equal to the maximum amount of funds to be held at any one time).

Payment of the bond premium may be made

by the district. If a tax collector refuses to provide a bond, the board may designate another proper person as tax collector.

The purpose of a bond is to insure the district against the loss of funds through fraud, theft or neglect as a result of the individual's actions.

CONSTRUCTION OF FACILITIES

Local school boards are charged with providing necessary grounds and suitable buildings to accommodate all school-age children in the district. This authority also includes the renovation and expansion of existing facilities, along with the construction of new buildings.

The process of school construction requires careful assessment of needs and the usability of existing facilities. Assessment of needs includes the projection of pupil enrollments.

The process of school construction requires careful assessment of needs and the usability of existing facilities. Assessment of needs includes the projection of pupil enrollments. Very careful planning and execution of construction programs is essential.

School building projects may be financed in a variety of ways:

Local Authority – The school board may establish an authority which in turn issues bonds and makes payments with funds provided by the district. Under this arrangement, the authority leases the building to the district for the life of the bond issue and then conveys the facility to the district at the end of that period. Lease payments are equal to the authority bond repayment schedule.

State Authority – School districts also may secure funding from the State Public School Building Authority, which issues the bonds and leases the facility to the district for the duration of the bond issue. Payment schedules are established by the state authority.

General Obligation Bonds – The most common practice is for a school board to directly issue its own bonds or notes, make payments and hold title to the school building. This is done in accordance with the provisions of the Local

Government Unit Debt Act, which establishes procedures and limitations on bonded indebtedness for school districts and municipalities.

Local Funds – Depending on the size of the project, a school board may opt to pay the cost of construction from current operating revenues of the district, thereby avoiding any long-term debt or financial obligations.

In most instances, school districts seeking state reimbursement for school construction projects are required to participate in PlanCon, an acronym for the PDE's Planning Construction Workbook. The process involves a number of phases, beginning with a definition of the project and justification of its need. Succeeding steps include: site approval; estimated project cost data; architectural reviews; cost data based on actual bids and, finally, approval of the bond issue or other funding mechanism. Specific requirements are detailed in regulations adopted by the State Board of Education and in standards promulgated by PDE.

School boards are required by Act 34 of 1973 to conduct public hearings. A second hearing is required if the bids received for a construction project exceed the initial PDE approved estimates by 8%.

Act 34 also is referred to as the "Taj Mahal Law," because it requires voter approval of any building project that exceeds per-pupil cost figures that are revised annually to reflect changes in the cost of living. Alterations to existing buildings are excluded from this requirement.

The School Code and other laws contain many specific requirements and should be studied carefully.

CAPITAL BUDGETING

Replacement of major items of equipment and significant repairs to buildings require careful planning. One of the more accepted practices is through a capital budget. Procedures for estimation of expenditures are similar to those for an operating budget. Unlike an operating budget, a capital budget may cover more than one year. Authority to

spend funds for a capital project are the same as spending in an operating budget.

Financing capital budgets usually comes from two sources. One method is through borrowing for specific projects. The second is through transfer of unused operating funds (from fund balance). Some improvements may require using both sources of funds.

INSURANCE PROGRAMS

Insurance needs of school districts have the same purpose as personal insurance. Specifically, insurance is designed to protect the district's financial interests against unusual circumstances. Insurances require the same careful consideration as any other financial element.

Elements of insurance include consideration about deductibles, amounts of coverage and programs designed to minimize risk and exposure.

Various sections of the School Code authorize the purchase of insurances.

- Group employee benefits and travel-accident insurance for board members is authorized by Section 513.
- Purchase of fire and liability insurance is authorized by Section 774.
- Insurance for vehicles is authorized by Section 1362.
- Insurance for district athletic programs is authorized by Section 511.

Purchase of insurance from board members or any employees of the district is prohibited by the School Code. Fringe benefits are authorized for employees only.

FINANCIAL RECORDS

Most financial records of school districts are public records pursuant to the Pennsylvania Right-To-Know Law. As public records, they are open to public inspection by citizens of the commonwealth. Specifically included in the act are "any account,

voucher or contract dealing with the receipt or disbursement of funds." Also included are public records dealing with the use or disposition of services, supplies, materials, equipment or property.

Section 518 of the School Code requires the board to retain forever: the minute book, annual auditor's reports and annual financial reports. Other financial records are required to be retained for a period of not less than six years.

Retention of records related to payroll and employment taxes are subject to the regulations of the Internal Revenue Service.

Citizens may make copies of the financial records. Additionally, the district may establish reasonable fees for making copies of the documents.

Chapter 10

A History of Distressed School Districts

ORIGIN OF A PROBLEM

The concept of distressed in relation to the commonwealth's school districts originated in the early 1930s when serious problems arose in the area of school finance, particularly in the state's coal-producing areas. Districts during this time were unable to collect sufficient amounts of local taxes to meet the costs of operating their schools. At the same time, the General Assembly was finding it difficult to meet the financial demands of districts. A salary schedule for teachers had been mandated and salaries could not be reduced by districts except with legislative approval.

GRANTS IN AID

The problem had become so severe by 1933 that the General Assembly took action to provide assistance. Two forms of relief were enacted. First, districts were permitted to reduce salaries during the 1933-35 biennium to an amount not less than 90% of the salaries to which teachers were entitled during the 1932-33 school year. In addition, further reductions in teachers' salaries were permitted if the secretary of education approved. Five million dollars designated for assisting financially distressed districts was placed at the disposal of the secretary through the act. Thus began a program of aid in the form of 5,181 grants amounting to more than $26 million over a 26-year period from 1933 through 1959.

SPECIAL TAX LEVY AUTHORIZATION

The first action of the General Assembly designed

specifically to aid financially handicapped districts other than by grants of special aid monies was contained in Act 604 of 1951, which provided authorization for distressed districts to levy an additional tax of 10 mills. The Department of Education was given the duty, under this law, to determine through investigation the conditions for such authorization.

During the late 1950s, it became apparent that the additional tax of 10 mills was insufficient and, on June 18, 1959, Act 101 was signed by the governor. The law not only eliminated the special levy permission, but also completely lifted the ceiling imposed on the taxing powers of fourth class school districts.

DEFINITION OF DISTRESS

By late 1959, the General Assembly had become aware that many districts had begun to rely upon the state to solve their fiscal problems, rather than to take action themselves to eliminate deficits. These districts were still employing more teachers than enrollment warranted, were not levying the maximum tax rate permitted by law or, if they had a high tax rate, were failing to collect the taxes. Some districts had, in fact, even included amounts for distressed aid in their annual budgets. A new approach to the problem of distressed school districts would have to be tried.

A new law – Act 675 – was signed by the governor in December 1959. The law both defined a distressed school district and delineated the circumstances through which a district would be declared distressed. A special board of control was provided for in the law to administer the affairs of the distressed district until such time as a sound fiscal structure was re-established. The secretary of education was given authority to declare a district distressed and to petition the Court of Common Pleas in the county in which the district was located for the appointment of two citizens to serve on the special board. The chairman of the special board would be appointed by the secretary. At the same time, the Justice Department ruled

that, from this time forward, only those districts officially declared distressed under the new law would receive grants of special aid.

Thus the pattern for distressed districts changed. No longer would districts receive monies under distressed conditions only to resort to prior poor management and fiscal methods once the money was received. Now the special boards would carry out the necessary steps to restore financial stability to these districts.

During the early '60s, the problem of distressed school districts centered predominantly in the anthracite coal areas of Cambria, Lackawanna, Luzerne, Northumberland and Schuylkill counties. By 1963-64, 36 districts were under distressed status declaration through Act 675.

The pattern for distressed districts changed. No longer would districts receive monies under distressed conditions only to resort to prior poor management and fiscal methods once the money was received. Special boards would carry out the necessary steps to restore financial stability.

REDUCTIONS IN DISTRESSED DISTRICTS

After that time, the numbers of distressed school districts in the commonwealth began to dwindle, due mainly to school district reorganization, liquidation of debts and overall improved economic conditions. Despite the improved economy and gains in employment patterns, however, pockets of depression and economic distress remained in various parts of the commonwealth.

By January 1972, three districts were declared distressed – General Braddock Area in Allegheny Co., Western Beaver Co. in Beaver Co. and Bethlehem Center in Washington Co. The last of these districts to remain distressed – General Braddock – was returned to the full control of the locally elected board of school directors on Feb. 14, 1974.

Some 10 years later, one additional school district – Clairton City in Allegheny Co. and part of the economically depressed Mon Valley Area – was declared distressed. The apex of the board of control's involvement was the renovation of the old high school building, with appropriate additions,

to house all children in grades K-12. The district was returned to local control in May 1988, after the dedication of the Clairton Education Center.

RECENT DEVELOPMENTS

In 1993, two districts are under distressed declaration – the Sto-Rox and Clairton City in Allegheny Co. Sto-Rox was declared distressed on May 22, 1992, after the elected board indicated it would not take the actions that were necessary to reduce the district's enormous deficit.

Clairton City was declared distressed for the second time within a decade on March 9, 1993. It had experienced an enormous decline in its total assessed valuation and a resulting loss in local revenue.

Both districts are governed by boards of control.

CRITERIA TO DETERMINE DISTRESS

Section 691 of the School Code establishes seven criteria for a declaration of distress. Only one of the criteria needs to be met for certification by the secretary of education. The criteria are:

- Salaries of any teachers or other employees have remained unpaid for 90 days.
- Tuition due another school district remains unpaid on and after January 1 of the following school year.
- Any amount due any joint board of school directors remains unpaid for 90 days.
- The district defaults payment on its bonds or interest on such bonds for 90 days.
- The district has contracted a loan not authorized by law.
- The district has accumulated and has operated with a deficit equal to 2% or more of the assessed valuation of the taxable real estate.
- A new district is created composed of a previously distressed district.

However, no school district shall be deemed to be distressed by reason of any of the cited circumstances if the commonwealth fails to make any payment of money due to the district at the time such payment is due.

POWERS AND DUTIES OF A BOARD OF CONTROL

A board of control is granted authority to take appropriate and necessary action (Sections 693, 694, and 695). Among the actions required are those conferred by law on the board of school directors. Once a board of control is appointed, school boards have no authority to act without the approval of the board of control.

Once a board of control is appointed, school boards have no authority to act without the approval of the board of control.

Another duty of the board of control includes requiring the school board to revise the district budget within 60 days to make such changes necessary to improve the financial condition.

To improve financial conditions, the board of control may require the school board to:

- Cancel or renegotiate any contract, other than teachers' contracts, to which the board is a party.
- Increase tax levies in amounts and at such time as required by law.
- Appoint a special collector of delinquent taxes.
- Direct the special school auditors of the department or appoint a competent independent public accountant to audit the accounts of the distressed school district.
- Dispense with the services of such nonprofessional employees as deemed are not actually needed for the economical operation of the school system.
- Suspend, in accordance with Section 1124, such number of professional and temporary professional employees as may be necessary to maintain a pupil-teacher ratio of no less than 26 pupils per teacher for the combined elementary and secondary enrollment.

Additional taxes may be levied by the regular board with the approval of the board of control. If the regular board fails to do so, the board of control may request the court to do so. Tax limits imposed by the School Code do not apply to a distressed school district.

Section 695 forbids school directors to resign from office, except with the unanimous consent of the special board, unless removed from office for neglect of duties under Section 318 by the court of common pleas. This process shall not interfere with any regular election or re-election of school directors for the district.

Appendix

- BIBLIOGRAPHY
- PENNSYLVANIA PUBLIC SCHOOL CODE OF 1949
- EXHIBIT 1 – SAMPLE POLICIES
- EXHIBIT 2 – VITAL STATISTICS ON BUDGET DECISIONS
- EXHIBIT 3 – BUDGET REVIEW AND ANALYSIS
- EXHIBIT 4 – GUIDELINES FOR AUDITING STUDENT ACTIVITY FUNDS
- GLOSSARY

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ARTICLE VI
SCHOOL FINANCES

(a) GENERAL PROVISIONS

Sch 601 Information to incoming directors for tax levy and budget
Sch 602 Tax levies
Sch 603 Only one annual tax levy
Sch 604 Property acquired by state for water conservation or flood prevention
Sch 605 Affidavit of uncollectibility of taxes on real property
Sch 606 Collection of taxes where new district created
Sch 607 Payments; how made; limitations
Sch 608 Liability for improper school orders
Sch 609 Budgeted funds not to be used for other purposes or exceeded
Sch 610 Use of School funds; illegal use
Sch 611 Enforcement of judgments against school districts
Sch 612 Counsel fees on appeals from county auditors' reports

(b) SCHOOL DEPOSITORIES

Sch 621 Designation of depositories; bond
Sch 622 Collateral in lieu of bond
Sch 623 Insurance of deposits of funds
Sch 624 Monthly reports by depositories
Sch 625 Deposit of school funds; treasurer relieved of liability; school orders

(c) INDEBTEDNESS

Sch 631 Power to incur debt; limitations
Sch 632 Assent of electors; when necessary and when not necessary
Sch 633 Reports to secretary of education; withholding state appropriations
Sch 634 Temporary debt
Sch 635 Limit on temporary debt for current expenses and debt service
Sch 636 Emergency loans for current expenses and debt service
Sch 637 Limit on temporary debt for permanent improvements, etc.; tax levy

Sch 638 Repealed
Sch 639 Limit on temporary debt in anticipation of proceeds of bond issue; payment
Sch 640 Borrowing in anticipation of current revenue

(d) FIRST CLASS SCHOOL DISTRICT

Sch 651 Fiscal year
Sch 652 Tax levy; purposes; limitations
Sch 652.1 Taxing power of elected board of public education of school districts of the first class A
Sch 652.2 Appeals by taxpayers
Sch 653 Tax levy for indebtedness of prior districts
Sch 654 Tax rates to be expressed in dollars and cents
Sch 655 Property taxable
Sch 655.1 Tax on owners of ground rents
Sch 656 Certification of assessments
Sch 657 Certification of levy; collection
Sch 658 Bond of collector; neglect to furnish
Sch 659 Compensation; stationery; books; clerks
Sch 660 Monthly reports; payment of taxes collected
Sch 661 Annual reports
Sch 662 Liens of unpaid taxes
Sch 663 Repealed
Sch 664 Annual budget; advertising; public hearing
Sch 665 Emergency appropriations
Sch 666 Limit of indebtedness

(e) SECOND, THIRD, AND FOURTH CLASS SCHOOL DISTRICTS

Sch 671 Fiscal year
Sch 672 Tax levy; limitations
Sch 672.1 School districts lying in more than one county or in more than one municipality; limitation on total tax revenues
Sch 672.2 School districts lying in more than one county; tax levy on occupations
Sch 673 Tax rates to be expressed in dollars and cents
Sch 674 Property subject to tax; districts second class
Sch 675 Certification of assessments, etc.; districts second class
Sch 676 Property subject to tax; districts third and fourth class
Sch 677 Certification of assessments, etc.; districts third and fourth class
Sch 677.1 Additions and revisions to duplicates
Sch 678 Duplicates to include certain territory
Sch 679 Per capita taxes
Sch 680 List of residents for per capita tax purposes
Sch 681 Certification of levy
Sch 682 Tax duplicates and warrants

Sch 683 Appointment of tax collector in certain cases
Sch 684 Bond of appointed collectors
Sch 685 Disqualification for reappointment, etc.
Sch 686 Delinquent taxes; appointment of collector; etc.
Sch 687 Annual budget; additional or increased appropriations; transfer of funds

(f) CAPITAL RESERVE FUND FOR SCHOOL BUILDING PROJECT PROGRAMS APPROVED BY THE DEPARTMENT OF PUBLIC INSTRUCTION

Sch 690 Creation of capital reserve fund for approved school building project programs
Sch 691 Investment of fund; budget; record
Sch 692 Expenditure of fund

(f) DISTRESSED SCHOOL DISTRICTS

Sch 691 When district distressed
Sch 692 Special board of control; petition; appointments
Sch 692.1 When no appointment is made
Sch 692.2 Compensation of special board of control
Sch 693 Powers of special board of control
Sch 694 Additional tax
Sch 695 School directors to remain in office; elections

OTHER SCHOOL CODE REFERENCES

Sch 318 Removal for failure to organize or neglect of duty
Sch 404 Districts second, third and fourth class permanent organization; election of officers
Sch 407 Rules and regulations
Sch 409 Payment of premiums on officers' bonds by school districts
Sch 431 Bond
Sch 432 Compensation
Sch 433 Duties
Sch 434 Assistant secretary
Sch 436 Bond
Sch 438 Compensation
Sch 439 Receipt and payment of school funds
Sch 440 Deposit of funds; monthly reports
Sch 440.1 Investment of school district funds
Sch 508 Majority vote required; recording
Sch 511 School athletics, publications, and organizations
Sch 513 Group insurance contracts
Sch 518 Retention of records
Sch 701 Duty to provide: conditions
Sch 731 Approval by department of plans, etc., of buildings exceptions
Sch 774 Insurance on buildings; public liability insurance for employes; purchase of insurance from employes, etc.

School Code

Sch 801 Purchases; use in schools; rules and regulations
Sch 807.1 Purchase of supplies
Sch 1124 Causes for suspension
Sch 1362 Kinds of transportation; liability insurance
Sch 2553 Audits and verifications of rights to reimbursements

EXHIBIT 1

SAMPLE POLICIES Page 1 of 3 **PAYMENT OF CLAIMS**

No. 616

SECTION: FINANCES

TITLE: PAYMENT OF CLAIMS

ADOPTED:

REVISED:

PSBA POLICY GUIDES FOR PENNSYLVANIA SCHOOLS

	616. PAYMENT OF CLAIMS
1. Purpose	It is the purpose of the Board to effect the prompt payment of bills, but at the same time to ensure that due care has been taken in the review of such bills.
2. Authority SC 439, 607, 1155	Each bill or obligation of this Board must be fully itemized, verified and passed upon by the Board before a check can be drawn for its payment, except that the Secretary is permitted to draw payment orders for:
SC 427, 439	☐ items the prompt payment of which will accrue to the advantage of the district ☐ progress payments to contractors as specified in a contract approved by the Board ☐ orders to cover approved payrolls and agency account deposits ☐ utility bills in months during which the Board does not meet.
3. Delegation of Responsibility	It shall be the responsibility of the ☐ Secretary ☐ Business Manager upon receipt of an invoice to verify that the purchase invoice is in order, the goods were received in acceptable condition or services were satisfactorily rendered, funds are available to cover the payment, the item is one for which the Board budgeted, and the invoice is for the amount contracted.
	Page 1 of 3

Exhibit 1

6.16. PAYMENT OF CLAIMS - Pg. 2

Should the invoice vary from the acknowledged purchase order, the _____ shall document on the invoice the reason for such variance.

SC 607, 687(d)

☐ Should funds not be available in the account to which a proposed purchase will be charged, the _____ shall determine the overage and request the Board make a legal transfer to cover it.

All claims for payment shall be submitted to the Board

☐ in the form of a listing including

- ○ check number
- ○ check date
- ○ to whom paid
- ○ amount of remittance
- ○ reason for remittance
- ○ account charged

☐ in the form of original records including a copy of the purchase order, the receiving report, the purchase invoice, and the purchase requisition.

☐ The check list shall be placed in the official minutes of the Board.

Prior to the Board's consideration of the bills for payment

☐ each invoice

☐ each invoice in excess of $

shall be reviewed by the _____.

SC 439

Upon approval of an order, the _____ shall prepare a check for payment, and cancel the commitment placed against the appropriate account.

SC 427, 433

All checks approved by the Board shall be signed by the President

☐ and Secretary.

Exhibit 1

616. PAYMENT OF CLAIMS - Pg. 3

SC 428

Act 276 of 1974

☐ The Vice-President may sign for the President.

☐ Signatures of the President and Secretary may be engraved on a signature plate

○ which shall be secured by the _____.

☐ Signatures of the President and Secretary may be engraved on a stamp

○ which shall be secured by the _____.

☐ No check shall be made out to cash.

School Code
427, 428, 433, 439, 607, 608, 610, 625, 687(d), 1155

Other Cites
Act 276 of 1974

Exhibit 1

SPECIAL PURPOSE FUNDS

No. 618

SECTION: FINANCES

TITLE: SPECIAL PURPOSE FUNDS

ADOPTED:

REVISED:

PSBA POLICY GUIDES FOR PENNSYLVANIA SCHOOLS

618. SPECIAL PURPOSE FUNDS

1. Purpose

It is the purpose of this policy to establish financial supervision and controls for the administration of the various activities that involve Special Purpose Funds.

2. Authority

The Special Purpose Funds of this district are

Name of Fund	Responsible Title
_____	_____
_____	_____

SC 511(d)

Student Body Funds are not part of district funds but shall be supervised by _____, approved by the Board, and who countersign all checks drawn upon them.

3. Definition

For purposes of this policy, the Student Body Fund(s) shall include the following activities:

- ☐ student government
- ☐ student clubs
- ☐ student entertainments
- ☐ student publications
- ☐ school classes
- ☐ school band
- ☐ school orchestra.

Other Special Purpose Funds are

Pol. 808

school cafeteria

Exhibit 1

618. SPECIAL PURPOSE FUNDS - Pg. 2

SC 504

☐ interscholastic athletics fund

○ including PIAA-sponsored activities

○ including non-PIAA sanctioned activities.

Each student body activity covered by this policy must be recognized and budgeted by the finance committee of the student body organization before funds can be collected or disbursed in the name of said activity. Said Committee shall be composed of the

☐ school principal

☐ student body advisor

☐ appointed faculty members

☐ elected student body officers.

Other Special Purpose Funds shall be controlled and budgeted in accordance with this policy and Pol. 808.

SC 511

☐ It is the policy of the Board to help defray the costs of the following activities:

○ student government

○ student clubs

○ student entertainments

○ student publications

○ school classes

○ school band

○ school orchestra

SC 504

○ school cafeteria

○ interscholastic athletics.

All other activities shall be on a self-sustaining basis.

Exhibit 1

618. SPECIAL PURPOSE FUNDS - Pg. 3

4. Guidelines

In order to ensure proper supervision of all Special Purpose Funds using the name of the school, the Board establishes the following guidelines:

☐ Funds of any student body organization may be deposited or invested in

- ○ banks whose accounts are insured by FDIC
- SC 440.1 ○ investment certificates or withdrawable shares in State-chartered savings and loan associations doing business in-State and insured by FDIC or FSLIC.

☐ Funds collected shall be turned in to the

- ○ Building Principal
- ○ Treasurer of the Fund
- ○ Custodian of the Fund

before the end of each school day, to be safeguarded until they are deposited as soon thereafter as possible.

SC 504 ☐ Funds from the cafeteria activities shall be treated as prescribed in Pol. 808.

☐ Funds from interscholastic athletic activities shall be under the supervision of the

- ○ Principal
- ○ Athletic Director
- ○ Secretary.

SC 511 Records shall be maintained of the receipt and disbursement of all such funds in designated accounts according to the activity involved.

Disbursements from such funds shall be made by check only upon the request of the authorized advisor and the approval of the

- ☐ Superintendent
- ☐ Secretary
- ☐ Business Manager

Exhibit 1

☐ Building Principal

☐ Treasurer of the Fund

☐ Custodian of the Fund.

All checks shall be signed by the person authorized to approve such disbursements.

SC 511(e)

Contracts for materials or supplies whether on purchase or rental may be made for a one-year period only by the

☐ Superintendent

☐ Secretary

☐ Business Manager

☐ Building Principal

☐ Treasurer of the fund

☐ Custodian of the fund.

☐ All funds should be of an exchange nature and large balances should not be permitted to accumulate. Money should not be raised or collected unless there is a definite purpose for doing so.

☐ No funds shall be expended without the approval of the faculty advisor of the organization, a student representative of the organization and

○ the principal (or)

○ other employe or school official _____.

All funds accumulated in the name of a specific activity must be closed out annually and any residual funds shall

☐ revert automatically to the school district.

☐ be refunded to the members of the group.

SC 511(d)

A financial report of the condition of each Special Purpose Fund organization shall be submitted to the Board

☐ monthly

Exhibit 1

618. SPECIAL PURPOSE FUNDS - Pg. 5

School Code
440.1, 504,
511

Board Policy
No. 808

☐ quarterly

☐ periodically _____.

Exhibit 2

EXHIBIT 2

VITAL STATISTICS ON BUDGET DECISIONS

In making budget decisions, statistics are needed about the people the schools serve; about the resources of the district to support education; about the staff and facilities that make schooling possible; and about district levels of operation today, to know what schools should be – and might have to be – in the years ahead. Here are the types of statistics to ask for, along with some illustrations and questions districts might raise on the basis of statistical information.

1. People schools serve

Total population in district
Characteristics of the population
- By age group
- By ethnic and racial background
- By type of family
  - With children
  - Without children
  - Single-parent families
- By income
- Number of handicapped students and kinds of handicaps

Population trends in the district
- Increasing
- Decreasing
- Change in socio-economic backgrounds
- Change in ethnic character

School population
- Total number of students enrolled
- By elementary grades
- By secondary grades

Projections for five to 10 years
- By elementary grades
- By secondary grades

Trends in private school enrollment
Minority student enrollment
- By schools
- By grades

Illustration 1: Statistics show an increase in the number of residents age 45-55. Should the board increase funds for adult education?

Illustration 2: Projections show a sharp decline in secondary school students in the next 10 years. Should the board eliminate funds for a new high school wing which has been scheduled for construction?

Exhibit 2

2. Resources of the district

Assessed valuation of taxable property

Total revenue from local sources

Total state aid

Federal aid

Revenue projections for three to five years

Projected economic changes

Illustration 3: New economic indicators point to a rise in local tax revenue due to the unexpected location of a large factory in the community. Should the board set up fiscal contingency plans for an 8% increase in staff and for additional classrooms in the elementary schools?

3. Staff and facilities

Total number of teachers

- By age
- By tenure-nontenure
- By salary distribution
- By number of years experience

Administrative and supervisory staffs

- By age-tenure-salary
- By function

Total number of school buildings

- By age
- Physical condition
- Scheduled closings, by years
- Scheduled major repairs and renovations, by years

Inventories of equipment

Illustration 4: Statistics show two parallel trends: declining enrollments and a continuing rise in the age of teachers. Should the board set up a fund to encourage early retirement through bonuses and incentive plans?

Illustration 5: New school census facts reveal an unexpected rise in enrollment during the next four years. Must the board eliminate from the budget expected revenue from the sale and rental of buildings which had previously been scheduled for closing?

4. Levels of operation

Student-teacher ratios

- By elementary grades
- By secondary grades

Exhibit 2

Student-staff ratios
- By elementary grades
- By secondary grades

Class size
- By elementary grades
- By secondary grades

Core current expenditures
Expenditure per student in ADA (Average Daily Attendance)
- By elementary grades
- By secondary grades

Expenditure per student
- By operating expense
- For capital outlay
- For interest on school debt

Illustration 6: School-staff ratios point to an excess of administrators and central office staff. Should the board ask the superintendent to report on possibilities of reductions-in-force and the amount of possible savings for the next budget?

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EXHIBIT 3
BUDGET REVIEW AND ANALYSIS

The following questions may prove helpful in the budget review and analysis process:

- What are the roles of administration and board in the budget process?
- What is the role of the community in the budget building and review process?
- Has a public budget presentation been prepared that will explain the district's problems, programs and budget in terms the general public will understand?
- What is the timeline for budget construction, review, preliminary adoption, public presentation and final adoption by the board?
- What are the sources of district revenue?
- What influence does the district have on the amounts of its revenue and when received?
- What is the historical pattern of tax collection in the district?

Exhibit 3

- Have delinquent tax accounts been taken into consideration when building the budget? Full collection of real estate taxes is not likely in any year.
- What state subsidies are earned by the district? Which are most important and can anything be done to improve state sources of revenue?
- What is the historical pattern of budget dollars in relation to the cost-of-living index?
- What is the relationship of tax receipts to the cost-of-living index?
- What is the assigned assessment ratio and what is the actual ratio between assessed and market value on real estate?
- How does the district budget compare with districts of the same size, economic condition and other similar factors?
- What financial resources or contingency plans exist in the event of a fiscal emergency?
- What are the required course offerings of the district?
- What are the elective courses offered by the district?
  - What are the class size requirements?
  - Do these programs conform to board philosophy?
  - Are these programs needed by the community?
- What are the board requirements for class size?
- What type of organizational structure is in place for carrying out the educational program? Is this structure appropriate?
  - Department organization.
  - Teaching assignments.
  - Relationship between curriculum development and staffing.
- How does the teacher salary schedule work and what changes, if any, need to be made?
- How does the salary program of nonprofessional staff work and what changes, if any, need to be made?
- What is the cash balance of the district and how is it used to hedge against future financial problems or tax increases?
- How is district and building administration organized? Is it appropriate and cost-effective?
  - Duplication of duties?
  - Unneeded administrators?
  - Inefficient reporting procedures?
- What is the board philosophy regarding evaluation and compensation of administrators?
  - What organizational changes will take place within the next five years?

Exhibit 3

- What contracted professional services does the district require? Is this the most cost-effective way to operate?
  - Legal services.
  - Auditing services.
  - Tax collection services.
  - Data processing services.
- What is the board philosophy on pupil transportation?
  - Assignment of stops.
  - Length of time on school bus.
  - Safety standards.
- Has a study been done recently comparing the cost of contracted busing services versus district owned?
- Does the district work with other's in solving difficult transportation problems?
- What impact does school opening and closing have on the cost of nonpublic transportation?
- What costs are involved in transporting students for activity programs and athletics? Is there a better way to accomplish the objectives at a lower cost?
- What percentage of local income is paid in school taxes?
- How has the percentage of local income paid to schools over the past several years changed in relation to the cost of living?
- How have district costs changed in comparison to the cost of living?
  - Evaluate by areas of school program.
- Is the district making use of para-professionals? Is this a satisfactory arrangement? Is it cost-effective?
- Is a district census maintained properly?
  - For tax purposes.
  - For enrollment projections.
- Does the district have a five-year financial plan in place?
- Is each child being provided equally with the best educational opportunity attainable with existing resources?
- Are resources being reasonably distributed among schools in the district?

EXHIBIT 4

GUIDELINES FOR AUDITING STUDENT ACTIVITY FUNDS

Section 511 of the Public School Code empowers the board of school directors in every school district to establish reasonable rules and regulations for the control of student activity funds. This responsibility includes the raising

and disbursing of money, as well as the organization and effective supervision of the various clubs, groups and organizations.

Historically, the objective of the state audit has been to ensure that school districts have adopted reasonable policies and procedures, instituted adequate internal controls, and complied with applicable laws, regulations and court decisions. At present, the examination of student activity funds is a discretionary audit function. The decision to audit these student monies is made on a case-by-case basis.

AUDIT OBJECTIVE

To determine if student activity funds are properly controlled and in compliance with Section 511 of Public School Code.

ROUTINE AUDIT PROCEDURES

- Interview the activity fund custodian(s) and complete the activity fund internal control questionnaire.
- Obtain a complete list and purpose for each student activity account.
- Review all board policies and administrative procedures governing the organization, management, supervision, control and financing of student activity funds.
- Review all pertinent financial reports noting items such as deficit balances, questionable accounts and inactive accounts.
- Perform tests to determine propriety of receipts, disbursements, bidding and student participation.
- Verify that funds remain property of students until graduation.
- Review the handling of income generated from investment of student monies.
- Verify that appropriate accounting procedures are being used and that all transactions are supported by adequate documentation.
- Ensure that fund custodian(s) are properly bonded.

USEFUL PUBLICATION

In the absence of official guidelines from the Pennsylvania Department of Education, school business administrators and fund custodians may find it useful to consult *Student Activities Fund: An Administrators Guide to the Development of Effective Student Activities Fund Policies and Procedures*, published jointly by PASBO, PAESSP and PASA.

Glossary

Aa

Accrual Method of Reporting Taxes – Reflects taxes earned during reporting period rather than taxes collected and remitted.

Act 511 Taxes – Revenue received from the flat and proportional assessments made in accordance with Act 511 of 1965 (Local Tax Enabling Act). School districts of the first class or first class A are not empowered to levy taxes under the provisions of Act 511.

Actual Instructional Expense (AIE) – The net cost of instruction in a school district.

Ad Valorem Taxes – Taxes levied by a governing body on the assessed valuation of the real or personal property located within that governing body's jurisdiction.

Aid Ratio – The result of the formula which reflects a district's wealth in relation to all other districts in the state.

Aid to Families With Dependent Children (AFDC) – A federal program administered through the Department of Welfare.

Appropriated Surplus – The amount of free balance or surplus which the board appropriates as revenue. The effect is to reduce the amount to be raised through local real property taxes.

Appropriation – An authorization granted by the board of education or voters to make expenditures and to incur obligations for specific purposes. An appropriation is usually limited in amount for the time covered by the approved budget.

Approved Reimbursable Costs (ARC) – The maximum limit to the reimbursement a district can receive for pupil transportation.

Assessed Valuation – The official valuation of property for the purpose of taxation. The valuation is determined by the assessors of the district (see School Code).

Audit – An examination of records and documents to determine 1) that transactions which are contemplated or have been completed were appropriate; or 2) that all transactions were recorded properly, completely and accurately.

Average Daily Attendance (ADA) – The total days of pupil attendance of a given school district during a reporting period, divided by the number of days school is in session during this period.

Average Daily Membership (ADM) – Aggregate number of school days represented by all pupils on the active roll divided by the number of days school is in session.

Bb

Base Earned for Reimbursement (BER) – Calculated reimbursement for instruction based on cost of instruction and the local tax effort.

Basic Instructional Subsidy (BIS) – A payment that includes: payment on account of instruction, payment on account of low-income families and payment on account of poverty.

Bond – A written promise to pay a specified amount of money at a certain time in the future and carrying interest at a fixed rate. The interest is usually payable periodically as specified in the bond. The term "bond" applies also to an insurance document guaranteeing the faithful performance of an official in assigned duties, and indemnifying the school district for financial loss resulting from unfaithful performance.

Budget – A complete financial forecast for a given time (usually one year) including both expenditures and receipt, based on an educational plan.

Budget Calendar – A guide for indicating budget preparation responsibilities and the dates for their accomplishment by individuals or groups.

148

Budgetary Transfers – Transfer of unencumbered funds or funds designated for one purpose to another part of the budget to be used for a different purpose, requiring approval by two-thirds of board members and allowed only during the last nine months of the fiscal year.

Cc

Capital Outlay – Expenditures for fixed assets or additions to fixed assets. They are expenditures for land, improvements to the grounds, construction of buildings, additions to or remodeling of existing buildings and initial or additional equipment.

Capital Reserve Fund – A special fund created for the purpose of constructing a school building project or projects under a long-term project program approved by the Department of Education.

Chart of Accounts – A list of all accounts used in an individual accounting system. An account is a descriptive heading under which are recorded similar financial transactions.

Current Expenditures (Current Expend) – Includes all general fund expenditures with reference to the functional classifications of: instruction (less tuition), support services, and operation of noninstructional services.

Dd

Debt Margin – The difference between the indebtedness of a school district and the amount of indebtedness which it can legally incur.

Debt Service – The expenditures for the retirement or paying off of the principal amount of a debt and the interest on the amount.

Default – When a school district fails to pay the interest and/or principal upon a bond when due, it is said to be in default, which is a failure to meet an obligation or to perform what has been promised.

Ee

Employee Benefits – A form of compensation in addition to salary for an employee. Such benefits include retirement benefits, Social Security, workers' compensation, sick leave, life insurance, accident insurance, disability insurance, etc.

149

Encumbrances – Purchase orders, contracts and salary or other commitments that are chargeable to an appropriation and for which a part of the appropriation is reserved.

Equalized Mills (EM) – A measure of the local tax effort calculated by dividing the local taxes by the market value multiplied by 1,000.

Exemption – A release from the obligation of having to pay taxes on all or part of the assessed value of a parcel of real property. When an exemption is granted, the rest of the owners of taxable property in the taxing unit must pay the taxes that would otherwise have been paid by the exempt property.

Fiscal Dependence – A legal condition in which some governmental unit other than the board of education has legal authority to approve or disapprove a budget after it has been prepared by the board.

Fiscal Independence – The legal condition that authorizes the local board of education to adopt its own budget directly or by submitting it to a direct vote of the qualified voters of the school district.

Fiscal Year – School districts of the first, first class A and second class may, by majority vote, establish a fiscal to coincide with the calendar year; all others shall begin July 1.

Fixed Charges – Expenditures which generally recur with some regularity such as retirement, Social Security, insurance, etc.

Fringe Benefits – See Employee Benefits.

Full Valuation – The current market value appraisal or estimate of what a property would sell for in a transaction between a willing buyer and a willing seller.

Function – Budgetary term used to describe the major purpose and the end an appropriation is to accomplish.

Functional Budget – A budget that uses the format of the line item or traditional budget to group proposed expenditures first according to general activities or actions performed. The major functional categories are: administration, instruction, pupil personnel services, pupil transporta-

tion services, health services, operation and maintenance of plant, etc. Within such functions, there are additional line items for various expenditures.

Fund – A fiscal and accounting entity for recording resources, liabilities and equity.

Gg

General Fund – The principal fund of a school district; includes all operations not required to be recorded in other funds, such as school lunch, capital reserves, activity funds, etc.

Generally Accepted Accounting Principles – An accounting system designed for use of local government units.

Ii

Independent Auditor – A certified public accountant or public accountant employed by the board of education to audit the financial records of the district for a fiscal year. The auditor or firm is usually engaged by annual contract at a fixed fee.

Invoice – An itemized list of merchandise purchased or services rendered from a particular seller or supplier of services; includes quantity, description, price, terms and date, etc.

Ll

Line Item or Traditional Budget – A budget that groups proposed expenditures according to certain categories known as the "object" of the expenditure. On each line of the budget, the expenses are listed the way they are paid out: salaries on one line, supplies on another line, utilities on another line. Thus salaries are one object and supplies another object.

Mm

Market Value (MV) – The value of taxable real property within a school district as determined by the State Tax Equalization Board.

Market Value Aid Ratio (MVAR) – A fraction used to calculate the state's share of instructional costs.

Market Value-Personal Income Aid Ration (MV-PIAR) – A factor used to determine the state's share of instructional costs.

Millage – The fixed rate of real estate taxes on assessed property value.

151

Oo

Object – The article to be purchased or the service to be obtained to carry out the function with which it is associated.

Objective – A specific description of an end result to be achieved; should tell what (end result), when (target date) and who (is accountable).

Operation of Plant – Expenditures necessary to keep the buildings and grounds and equipment open and ready for use – "Housekeeping" costs.

Pp

Personal Income Aid Ratio – A fraction used to determine the market value personal income aid ratio.

Program Budget – A program is a plan of activities or procedures designed to accomplish a set of related objectives. A program budget groups all the proposed expenditures for each individual program; then within each program, expenditures are listed according to function and object. A program budget includes the delineation or definition of the purpose or objectives of a particular program – that is, what that program is expected to accomplish. The dollar amounts budgeted are considered in relation to achieving a desired and agreed-to purpose.

Program budgeting differs from line-item budgeting in that it focuses on the purposes of the district and the particular program and activity. It is a variation from the concept of functional budgeting because in the latter the budget amounts requested are merely an itemization of the dollars required to continue a given activity or to install a new one. Moreover, a functional budget does not link program costs to program results.

Proposed Budget – A tentative budget subject to public hearings, examination or comment. When the district is fiscally dependent on another municipal body, such as the town or city council — for its funds, the proposed budget is sometimes called the budget request.

Purchase Order – A written request to a seller or vendor to supply merchandise or services in a given quantity at a given price and of a described quality.

Purchasing Agent – The person designated by the board of education to be responsible for purchasing, as required by commissioner's regulations.

152

Requisition – A written request to the purchasing agent for some specific materials, supplies, equipment or services.

Reserve Fund – An amount set aside to cover an obligation duly authorized and incurred.

Rr

Sinking Fund – Money set aside or invested for the definite purpose of meeting payments on debt at some future date; usually a fund set up for the purpose of accumulating money over a period of years to have money available for the redemption of long-term obligations at the date of maturity.

Ss

Tax Levy – The total dollar amount to be raised by tax.

Tax Rate/Mill – The tax levy divided by the total taxable assessed value of the district, usually stated as dollars per thousand or per hundred of assessed value.

Tt

Total Expenditures (Total Expend) – Includes all general fund expenditures cited under current expenditures plus facilities acquisition and other financing uses (less prior years' receipts and fund transfers).

Vv

Voucher – A document authorizing the payment of money for which the district has been billed. There is usually an indication of the account and the code number for bookkeeping entries.

Vocational Average Daily Membership (VADM) – Weighted pupils in Average Daily Membership in area vocational-technical schools and vocational curriculums in local school districts.

Ww

Weighted Average Daily Membership (WADM) – The number of weighted pupils in average daily membership. It is calculated by multiplying the Average Daily Membership by a differential weighting factor at each level of instruction.

Zero Base Budgeting – A method of budgeting that requires each person requesting funds in a budget to develop "decision packages" and to rank them in priority order.

Zz

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